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BEFORE THE ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION
DOCKET CONTROL

COMMISSIONERS
GARY PIERCE, Chairman
BOB STUMP
SANDRA D. KENNEDY
PAUL NEWMAN
BRENDA BURNS

IN THE MATTER OF THE APPLICATION OF GOODMAN WATER COMPANY, AN ARIZONA CORPORATION, FOR (i) A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND (ii) AN INCREASE IN ITS WATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.

DOCKET NO. W-02500A-10-0382

STAFF'S NOTICE OF FILING SURREBUTTAL TESTIMONY

The Utilities Division ("Staff") of the Arizona Corporation Commission ("Commission") hereby submits the Surrebuttal Testimony of Staff Witnesses Gordon L. Fox, Marlin Scott, Jr. and Juan C. Manrique in the above-referenced matter.

RESPECTFULLY SUBMITTED this 13th day of June, 2011.

Arizona Corporation Commission
DOCKETED
JUN 13 2011
DOCKETED BY

Ayesha Vohra

Ayesha K. Vohra, Staff Attorney
Bridget A. Humphrey, Staff Attorney
Legal Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007
(602) 542-3402

Original and thirteen (13) copies of the foregoing were filed this 13th day of June, 2011 with:

Docket Control
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Copies of the foregoing were mailed and/or emailed this 13th day of June, 2011 to:

Lawrence V. Robertson, Jr.
P.O. Box 1448
Tubac, Arizona 85646
Attorney for Goodman Water Co.
tubaclawyer@aol.com

Daniel Pozefsky
Chief Counsel
Residential Utility Consumer Office
1110 West Washington, Suite 220
Phoenix, Arizona 85007
dpozefsky@ruco.gov

Lawrence Wawryzniak
39485 S. Mountain Shadow Drive
Tucson, Arizona 85739
l.wawrzyniak05@comcast.net

James Schoemperlen
39695 S. Horse Run Drive
Tucson, Arizona 85739
JSchoemperlen@sargentaerospace.com

BEFORE THE ARIZONA CORPORATION COMMISSION

GARY PIERCE
Chairman
BOB STUMP
Commissioner
SANDRA D. KENNEDY
Commissioner
PAUL NEWMAN
Commissioner
BRENDA BURNS
Commissioner

IN THE MATTER OF THE APPLICATION OF GOODMAN WATER COMPANY FOR AN INCREASE IN ITS WATER RATES FOR CUSTOMERS WITHIN PINAL COUNTY, ARIZONA	))))))	DOCKET NO. W-02500A-10-0382

SURREBUTTAL

TESTIMONY

OF

GORDON L. FOX

PUBLIC UTILITIES ANALYST MANAGER

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

JUNE 13, 2011

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EXECUTIVE SUMMARY
GOODMAN WATER COMPANY
DOCKET NO. W-02500A-10-0382

Goodman Water Company ("Goodman" or "Company") is an Arizona for-profit, Class C public service corporation providing water service to approximately 600 customers in the vicinity of Oracle in Pinal County, Arizona. On September 17, 2010, Goodman filed a general rate application. The application shows that Goodman posted a $73,882 adjusted operating income for the test year that ended December 31, 2009. Goodman's application requests a $291,454 (50.9 percent) revenue increase to provide a $253,194 operating income for a 10.54 percent rate of return on a $2,402,222 fair value rate base. Goodman's rebuttal testimony requests a 262,717 (44.19 percent) revenue increase to provide a $227,309 operating income for a 9.89 percent rate of return on a $2,298,376 fair value rate base.

The surrebuttal testimony of Staff witness Mr. Gordon L. Fox addresses rate base, operating income, revenue requirement and rate design issues.

Staff's surrebuttal revenue requirement of $775,283 represents an increase of $180,824, or 30.24 percent, over test year revenue of $594,459 for a 9.2 percent rate of return on a Staff adjusted OCRB of $1,974,781. Staff's surrebuttal revenue requirement represents a $74,344 increase from its direct testimony. Staff's recommendation reflects eight rate base adjustments for a $427,441 reduction and seven operating income adjustments for a $1,735 increase in adjusted test year operating income.

The present rate structure for the residential, commercial, and construction customer classes consists of an inverted three-tier commodity rate for 5/8 x 3/4-inch and 3/4-inch meters. An inverted two-tier commodity rate structure applies to larger meters. A minimum monthly fixed charge that increases by meter size is also applicable to residential and commercial customers.

The Company rebuttal proposes a rate structure similar to the present rate structure that collects a greater proportion of the revenue from the commodity rates and spreads the rates between the tiers by a greater ratio by increasing the ratio between the first and second tiers for 5/8 x 3/4-inch and 3/4-inch meters. On average, the Company's proposed rates increase by 44.7 percent to achieve its proposed revenue requirement.

Staff's surrebuttal rate structure and the Company's rebuttal rate structure are similar with the same break-over points, similar percentages of revenue recovered through the monthly minimum charges and the commodity rates. Staff's recommended rate design would generate Staff's surrebuttal water revenue requirement of $775,283 composed of $761,545 from water services and $13,738 from other revenues. Staff's recommended rates would increase the typical residential water bill with median month usage of 4,500 gallons by $19.07, or 31.29 percent, from $60.96 to $80.03.

Rebuttal Testimony of Thomas J. Bourassa

Accounting Order for Depreciation on Excess Capacity - The Commission should deny the Company's request for an accounting order to defer depreciation expense on any plant the Commission excludes from rate base that represents excess capacity.

Land Parcels - Staff recommends valuing the four land parcels at the lower of the market price or net book carrying value by EC Development if and when the Company provides sufficient support for such a determination.

Rebuttal Testimony of James A. Shiner

Written Policies - Staff continues to advocate that the Company develop and implement written policies to guide the Company in affiliate and hiring of outside consultants.

Rebuttal Testimony of Michael J. Naifeh

Appraisal Comments - Staff retracts that portion of Mr. McMurry's direct testimony that states his appraisal was flawed. However, Staff does not recognize Mr. Naifeh as independent for the land parcel transactions or the Company. Mr. Naifeh's lack of independence neither suggests a concern of his abilities as an appraiser nor his personal integrity.

Rebuttal Testimony of John Ferenchak III

Appraisal Comments - Staff has no direct concern with accepting Mr. Ferenchak III's appraisal for the land parcels, and Staff has neither reason to doubt his abilities as an appraiser nor to question his personal integrity; however, the circumstances of the appraisal call for a professional level of skepticism.

Rebuttal Testimony of James Schoemperlen

Projected Returns - Mr. Schoemperlen correctly observes that since the mix of fixed and variable costs do not remain constant with customer/revenue growth, recognizing the plant values for capacity in excess of test year customers will result in growth in returns. However, the regulatory framework recognizes this benefit to utilities. The regulatory framework has both regulatory benefits and liabilities and regulators are challenged to find an optimal balance between the benefits and liabilities, not necessarily to eliminate them.

Rebuttal Testimony of James Wawrzyniak

Customer Communications - Staff has revised its reported statistical data to opinions and complaints. Mr. Wawrzyniak's testimony provides a summary of opinions and complaints filed with the Commission. This appears to be raw data. Staff has found individuals and households sometimes file multiple communications, and Staff's reported communications reflect removal of multiple opinions and complaints from a single individual or household. Accordingly, Staff's reported statistics will not agree with the raw data.

I. INTRODUCTION

Q. Please state your name, occupation, and business address.

A. My name is Gordon L. Fox. I am a Public Utilities Analyst Manager employed by the Arizona Corporation Commission ("ACC" or "Commission") in the Utilities Division ("Staff"). My business address is 1200 West Washington Street, Phoenix, Arizona 85007.

Q. Briefly describe your responsibilities as a Public Utilities Analyst Manager.

A. In my capacity as a Public Utilities Analyst Manager, I supervise analysts whose duties include preparation of testimonies to provide the Commission with Staff recommendations regarding rate base, operating income, cost of capital, rate design, securities issuance and other financial regulatory matters.

Q. Please describe your educational background and professional experience.

A. I have twenty years of regulatory utility auditing and rate analysis experience (17 years at the Commission and 3 years at RUCO) and four years of experience with a cable TV utility with responsibility for preparing and presenting rate applications before jurisdictional authorities. I have master and bachelor degrees in Accounting, and I have earned the following professional accounting and finance certifications: Certified Public Accountant ("CPA"), Certified Management Accountant ("CMA") and Certified in Financial Management ("CFM").

Q. Did you previously file direct testimony in this proceeding?

A. No. Staff's direct testimony regarding rate base, operating income, revenue requirement and rate design was filed by Mr. Gary T. McMurry. I am adopting Mr. McMurry's direct testimony as modified herein.

II. PURPOSE OF SURREBUTTAL TESTIMONY

Q. What is the purpose of your Surrebuttal Testimony in this proceeding?

A. The purpose of my Surrebuttal Testimony in this proceeding is to respond on behalf of Staff to the Rebuttal Testimonies of Goodman Water Company ("Goodman" or "Company") witnesses Thomas J. Bourassa, James A. Shiner, Mark Taylor, Michael J. Naifeh, and John Ferenchak III and to intervenors James Schoemperlen, and Lawrence Wawrzyniak who represent Southland Utilities Company, Inc. ("Southland" or "Company") and to present Staff's surrebuttal position regarding rate base, operating income, revenue requirement and rate design issues. Staff witness Marlin Scott is presenting the engineering analysis and recommendations. Staff witness Juan Manrique is presenting the cost of capital analysis and recommendations.

Q. Has Staff attempted to address every issue raised by the Company in its Rebuttal Testimony?

A. No. Staff's silence on any particular issue raised in the Company's or intervenors' Rebuttal Testimonies does not indicate that Staff agrees with the stated Rebuttal position on the issue.

Q. Have you prepared any schedules to accompany your testimony?

A. Yes. I prepared Surrebuttal Schedules GLF-1 to GLF-20. The surrebuttal schedules reflect the Company's application as filed, not its rebuttal position.

Q. How is your surrebuttal testimony organized?

A. My testimony is presented in five sections. Section I is the introduction. Section II is this description/purpose of my testimony. Section III provides a background of the Company. Section IV is a summary of consumer service issues. Section V is a summary of proposed revenues. Section VI is a summary of Staff's rate base and operating income adjustments. Section VII presents Staff's rate base recommendations. Section VIII presents Staff's operating income recommendations. Section IX discusses the Company's affiliated party transactions. Section X discusses rate design. Section XI presents my responses to the rebuttal testimony provided by Company witness Thomas J. Bourassa. Section XII presents my responses to the rebuttal testimony provided by Company witness James A. Shiner. Section XIII presents my responses to the rebuttal testimony provided by Company witness Mark Taylor. Section XIV presents my responses to the rebuttal testimony provided by Company witness Michael J Neifeh. Section XV presents my responses to the rebuttal testimony provided by Company witness John Ferenchak III. Section XVI presents my responses to the rebuttal testimony provided by intervenor James Schoemperlen. Section XVII presents my responses to the rebuttal testimony provided by intervenor Lawrence Wawrzyniak.

III. BACKGROUND

Q. Would you please review the pertinent background information associated with the Company's application for a permanent rate increase?

A. Goodman is a class C public service corporation that provides water service to approximately 600 customers in the vicinity of the town of Oracle in Pinal County, Arizona. On September 17, 2010, Goodman filed an application for approval of permanent rates and charges for water service, and on November 5, 2010, Staff filed a letter declaring the application sufficient. Goodman's application asserts that an increase in revenues is required to recover operating expenses and to provide debt service coverage and a 10.54 percent return on fair value rate base ("FVRB").

Q. What test year did Goodman use in its filing?

A. Goodman's rate filing is based on the twelve-month period that ended December 31, 2009.

Q. When were Goodman's present rates established?

A. The Commission Decision No. 69404, dated April 16, 2007, granted the Company its present permanent rates.

Q. Does Goodman have any other cases currently pending before the Commission?

A. No.

IV. CONSUMER SERVICE

Q. Please provide a brief summary of customer complaints received by the Commission regarding Goodman Utilities.

A. Staff reviewed the Commission's records for the period January 1, 2008, through March 7, 2011, and found the following: 2008 - one complaint (billing); 2009 - one complaint (billing); 2010 - zero complaints, 245 individual opinions opposed to the rate increase and one petition with 22 signatories; and 2011 – one complaint and three opinions opposed to the rate increase.[1] The Company is in good standing with the Corporations Division. The Company is current on all property and sales taxes.

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[1] The reported communications reflect removal of multiple opinions and complaints from a single individual or household.

V. SUMMARY OF PROPOSED AND RECOMMENDED REVENUES

Q. What rebuttal revenue requirement is Goodman proposing?

A. The Company's rebuttal testimony proposes total operating revenue of 857,176,[2] an increase of $262,717, or 44.19 percent, over its test year revenue of $594,459. The Company's rebuttal request claims to provide an operating income of $227,309 for 9.89 percent rate of return on a $2,298,376 fair value rate base ("FVRB") which is the same as the proposed original cost rate base ("OCRB").

Q. Please provide a summary of Staff's surrebuttal recommendations.

A. Staff's surrebuttal revenue requirement of $775,283 represents an increase of $180,824, or 30.42 percent, over test year revenue of $594,459 for a 9.2 percent rate of return on a Staff adjusted OCRB of $1,974,781. This surrebuttal revenue requirement represents a $74,344 increase from Staff's direct testimony. Staff's recommended rates would increase the typical residential water bill with median month usage of 4,500 gallons by $19.07, or 31.29 percent, from $60.96 to $80.03.

Q. Explain the primary reasons that Staff's surrebuttal revenue requirement differs from that in its direct testimony.

A. Staff's surrebuttal position reflects the following modifications to its direct position: the rate of return increased from 9.0 percent to 9.2 percent due to an increase in the cost of equity from 9.1 percent to 9.3 percent; operating revenue increased by $14,349; operating expenses by $22,387; and rate base increased by $235,069.

Surrebuttal Schedules GLF-1 to GLF-20 present the detail and results of Staff's adjustments.

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[2] This is a $7,029 decrease from the $864,205 revenue requested in the rate application.

VI. SUMMARY OF STAFF'S RATE BASE AND OPERATING INCOME ADJUSTMENTS

Q. Please summarize Staff's rate base and operating income adjustments.[3]

A. Rate Base:

Land Purchase – This adjustment decreases the cost basis of the Company's 2008 land purchase by $379,837 because this non-arm's-length transaction was belatedly recorded and other factors.

Reclassify Water Treatment Plant – This adjustment reclassifies $15,947 in funds from G/L account 320 "Water Treatment Plant" to G/L account 320.2 "Chemical Solution Feeders."

Reclassify Distribution Reservoirs

This adjustment reclassifies $836,890 from G/L account 330 "Distribution Reservoirs" between two G/L accounts; 330.1 "Storage Tanks" and 330.2 "Pressure Tanks."

Remove cost of upsizing storage tank with excess capacity

This adjustment removes the $72,350 cost for a 190,000 gallon upsize of a water storage tank that Staff and the Company agree represents excess capacity.

Eliminate Transmission Mains

This adjustment eliminates $128,600 from transmission mains to reflect lines that Staff has deemed to be not used or useful.

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[3] Unless stated otherwise, Staff's adjustments throughout the testimony are to the Company's application, not to its rebuttal position.

Adjust accumulated depreciation

This adjustment decreases the accumulated depreciation balance by $7,910 to reflect Staff recommended plant values.

B. Operating Income:

Revenue Annualization – This adjustment increases test year revenues by $21,708 to recognize customer growth during the test year in agreement with the Company's rebuttal testimony.

Annualize Purchased Power Expense – This adjustment increases purchased power expense by $577 to reflect the increase in cost associated with the increased water sales from annualization of revenues, and it adopts the amount requested by the Company in its rebuttal testimony.

Rate Case Expense – This adjustment increases rate case expense by $20,000 to reflect a normalized amount of $40,000 which is the annual amount requested by the Company in its rebuttal testimony.

Water Testing Expense – This adjustment increases water testing expense by $1,568 to reflect Staff's recommended water testing expense. The Company's rebuttal testimony adopts Staff adjustment.

Depreciation Expense – This adjustment increases depreciation expense by $11,047 to reflect application of Staff's recommended depreciation rates to Staff-recommended plant amounts.

<u>Property Taxes</u> – This adjustment decreases test year property taxes by $2,250 to reflect application of the modified version of the Arizona Department of Revenue's property tax methodology which the Commission has consistently adopted.

<u>Test Year Income Taxes</u> – This adjustment decreases test year income tax expense by $9,496 to reflect application of statutory state and federal income tax rates to Staff-adjusted taxable income.

VII. RATE BASE

Fair Value Rate Base

Q. Does Goodman's application include schedules with elements of a Reconstruction Cost New Rate Base?

A. No. The Company's application does not request recognition of a Reconstruction Cost New Rate Base. Accordingly, Staff has treated the Company's OCRB as its FVRB.

Rate Base Summary

Q. Please summarize Staff's surrebuttal rate base recommendation.

A. Staff recommends a $1,974,781 FVRB, a $427,441 reduction from the $2,402,222 rate base proposed in the application, and it is $323,595 less than the Company's $2,298,376 rebuttal testimony rate base. Staff's recommendation results from the rate base adjustments described below.

Rate Base Adjustment No. 1 – Reduce Cost Basis for Land Purchase

Q. What did the Company propose in its application with respect to land in the test year?

A. Schedule B-2, page 3, line 7, of the Company's application shows that the Company recorded a balance in the land and land rights account of $494,159. The entire balance was due to the 2008 purchase of four parcels of land from an affiliated party, EC Development, Inc.

Q. Did the Company's rebuttal testimony propose a modified value for the land?

A. Yes. The Company's rebuttal reduced the land value by $35,000 to $459,159.[4]

Q. Is there any reason to question the value the Company used to record the land?

A. Yes. Staff has identified multiple reasons to question the recorded value of the land. First, the transaction was not recorded at cost at the time the land was placed in service. Second, the transaction was not at arm's length, and the Company has not shown that the transaction was recorded in accordance with NARUC audit guidelines for affiliate transactions. Third, the land appraisal used to value the transaction was conducted by an appraiser that was not independent from the Company.

Q. Did the Company record the land in its records on the date that the land was devoted to public service?

A. No. The Company recorded the acquisition of four land parcels in its general ledger on October 31, 2008.[5] The Company provided the following dates for property on land: parcel one, June 2003; parcel two, 2004 & 2005; parcel three, 2007 & 2008; and parcel

[4] Bourassa rebuttal p. 3 and Schedule B-2, p. 3.
[5] Company response to Staff data request 4.13.

four, June 2003.[6] According to this Company provided information, each of the four parcels was placed into service between one and five years prior to the recorded in-service date. Fixed assets should be recorded at the time it is devoted to public service.

Q. What caused the Company to delay recording the land until long after it was placed into service?

A. According to the Company, it was an inadvertent oversight at that point of time.[7]

Q. What is the relationship between the Company and the land seller?

A. Goodman purchased the four parcels of real estate from EC Development for $490,000. EC Development is owned by Alex Sears and James Shiner.[8] Mr. Sears and Mr. Shiner are both owners of Goodman. In response to Staff data request GTM-1.11, the Company identified EC Development, Mr. Sears and Mr. Shiner among others, as affiliates of the Company.

Q. What is the concern regarding non-arm's length transactions?

A. Non-arm's length transactions are suspect of self-dealing and may not be conducted at market price. The purchaser of the land, in this case, is related to the seller of the land. In such cases, it is not clear whether the price paid for the real estate was truly market value.

[6] Company witness Mr. Ferenchak III uses different and more precise dates in his appraisal as follows: parcel one, May 1, 2002; parcel two, August 1, 2005; parcel three, January 1, 2008; and parcel four, October 1, 2004.
[7] Mr. Bourassa rebuttal, p. 3 and Company response to Staff data request GTM-7.9.
[8] Company response to Staff data request 4.03.

Q. According to NARUC Guidelines for Cost Allocations and Affiliate Transactions ("Guidelines"), what is an appropriate basis for recording the transfer of a capital asset from an affiliate to a utility?

A. Generally, the transfer of assets from an affiliate to the utility should be at the lower of prevailing market price or net book value, and an appraisal should be used to determine the market price.

Q. What is Staff response to Mr. Bourassa's comments that "This document specifically states that the Guidelines are not intended to be rules or regulations prescribing how cost allocation and affiliate transaction are to be handled? Further, the Guidelines also state that the transfer of an asset from an affiliate to the utility should be at the lower of cost or prevailing market price or net book value, *except by law or regulation.* In that regard, the Commission rules require that assets be recorded at the cost to the person (or company) *first devoted to public service.* And, the cost is the *cost at the time the asset is devoted to public service.*"[9]

A. Apparently, Mr. Bourassa believes that the amount that is recorded in a non-arm's length transaction represents cost. The recorded amount in a non-arm's length transaction does not provide a reliable representation of market value or cost. The fundamental concern with affiliate transactions is that those transactions may not be recorded at a cost that represents market price. The Guidelines address this concern by suggesting that the appropriate amount to value affiliate transactions is the lower of market price or net book value.

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[9] Bourassa rebuttal, p. 5.

Q. Has the Company shown that the transaction for the land was recorded in accordance with NARUC audit guidelines for affiliate transactions?

A. No. The Company has not provided the book value of the land carried by the seller.

Q. Has Goodman been asked to provide the book value of the land carried by EC Development?

A. Yes. The following is the joint data request 5.01 from intervenors Mr. Wawrzyniak and Mr. Schoemperlen and Goodman's response.

> Question: Please supply the EC Development value of the four land parcels for the Water Plant and Wells that Goodman Water Company purchase from your affiliate EC Development in 2008.
>
> Response: Goodman Water Company objects to this question on the ground(s) that the information therein is irrelevant and it is unlikely to lead to the discovery of relevant information. What may be relevant is what the market value of the four (4) parcels in question was at the time(s) each was devoted to public service by Goodman Water Company; and that information was provided in the prepared Rebuttal Testimony of Goodman Water Company, which the Individual Intervenors have previously received.
>
> Finally, E.C. Development and Goodman Ranch Associates did not carry any specific land values on their respective books for the four (4) specifically-sized parcels which are the subject of this data request. Land values were carried for larger parcels of acreage, and those land values are both proprietary and irrelevant to this proceeding.

Q. Can Staff identify any reason why EC Development's carrying value of the four land parcels is relevant to this case?

A. Yes. As discussed above, according to the Guidelines, the transfer of assets from an affiliate to a utility generally should be at the lower of prevailing market price or net book value. Since the seller, EC Development, is an affiliate of the buyer, Goodman, it is necessary to have both EC Development's carrying value and the market value of the land parcels to determine the appropriate value to record the land parcels.

Q. Is Goodman relieved of its obligation to provide EC Development's carrying value of the land parcels purchased if the purchased parcels were subsections of larger parcels on EC Development's books?

A. No. Goodman has the obligation to provide appropriate support for the values it proposes. Goodman could have proposed a method for assigning or allocating portions of the larger parcel valuations to the parcels acquired.

Q. What did the Company use to determine the basis for the amount to record the land?

A. The Company recorded the land's acquisition price based on a Summary Appraisal Report performed by Michael Naifeh, MAI, CRE, dated June 26, 2008.

Q. Is an appraisal an appropriate method for valuing a land transaction?

A. Yes. Due to the unique nature of real property, a readily identifiable market price is not available for land; accordingly, an appraisal may be the best alternative.

Q. Who performed the appraisal to support the recorded value of the land parcels?

A. Mr. Naifeh prepared the appraisal dated June 26, 2008.

Q. Was Mr. Naifeh independent of the transaction to sell the land parcels?

A. Mr. Naifeh's rebuttal testimony asserts that: (1) Mr. Sears, an owner of Goodman, through D&D Investment West L.L.C. invested approximately $300,000 in a $19,000,000 property in Flagstaff; (2) Mr. Naifeh organized the investment group that purchased the Flagstaff property; and (3) Mr. Naifeh has prepared less than five appraisals directly for Mr. Sears.[10] Thus, Mr. Naifeh has an indirect relationship with the land transaction and a historical business relationship with Mr. Sears. In fact, Mr. Naifeh disclosed in his appraisal that he had a financial interest related indirectly to the transaction. Accordingly, Mr. Naifeh is not independent of the transaction to acquire the land parcels.

Q. Does Mr. Naifeh's lack of independence mean that he engaged in any impropriety?

A. No. Staff is not suggesting that Mr. Naifeh did anything inappropriate. Staff is neither questioning his abilities as an appraiser nor his personal integrity. However, independence is a fundamental characteristic of objectivity. Therefore, Mr. Naifeh's lack of independence taints the appraisal. Mr. Naifeh's disclosure of his non-independence related to the transaction, professional dedication and commitments, certification that the appraisal was unbiased and the relatively small investments involved with the common interests are potential mitigating elements, but his lack of independence by its nature places some circumspection on the results.

Q. What is the basis for the Company's rebuttal land valuation of $459,159?

A. The Company's rebuttal testimony reduces the land valuation by $35,000 from $494,159 to $459,159[11] based on a appraisal dated April 29, 2011, performed by a different appraiser, Mr. Ferenchak III.

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[10] Naifeh rebuttal, p. 7.

[11] Closing costs, $2,159; Appraisal fee $2,000.

Q. Why did the Company request Mr. Ferenchak III to perform an appraisal?

A. The Company retained Mr. Ferenchak III to perform an appraisal to resolve both the issue of Mr. Naihef's independence and the date of valuation.[12]

Q. Is Staff aware of any reason to question that Mr. Ferenchak III is independent in relation to either the Company or the transaction?

A. No. Mr. Ferenchak III asserts that he has no present or prospective interest in the parcels and no personal interest with respect to the parties involved.[13] Staff is not aware of any reason to question that Mr. Ferenchak III is independent from the Company or the transaction.

Q. Does Mr. Ferenchak III's appraisal purport to provide an appraisal for the land parcels that match the dates that the parcels were committed to public service?

A. Yes. The appraisal purports to have provided evaluations consistent with the in-service dates of the land parcels, i.e., parcel one, May 1, 2002; parcel two, August 1, 2005; parcel three, January 1, 2008; and parcel four, October 1, 2004.[14]

Q. Does Staff have any reservations about accepting Mr. Ferenchak III's appraisal as the market value for the land parcels?

A. Staff has no direct concern with accepting Mr. Ferenchak III's appraisal for the land parcels, and Staff has neither reason to doubt his abilities as an appraiser nor to question his personal integrity.

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[12] Bourassa rebuttal, p.8.
[13] Fernenchak III rebuttal, Attachment A, p. 35.
[14] These dates are difference and more precise than the dates provided in response to Staff data request GTM-7.9.

Nevertheless, it would be remiss to ignore that the history (a non-arm's length transaction, not recorded at the time required by the USOA, and an initial appraisal by a non-independent appraiser) and that the circumstances provided the Company an incentive to obtain a high appraisal valuation for the land parcel and to seek to find an appraiser that would render a favorable conclusion. That is, the circumstances warrant application of a healthy level of professional skepticism. The need for skepticism is exacerbated by the Company's assertion that its failure to record the transactions at the time the parcels were devoted to public service was nothing more than an oversight[15] in consideration of the Company's description of the complexity of the transaction as ultimately executed in 2008. Goodman paid $2,000 for an appraisal, $2,159 for closing costs and it purchased the land for consideration of $271,000 (1.552 shares) in Goodman Water Company stock, $115,000 cash at close of escrow and $98,400 in seller financing.[16] These actions indicate that this was not a nonchalant transaction that would simply have been overlooked initially.

Q. Assuming that Mr. Ferenchak III's appraisal provides an accurate representation of the market value of the land parcel at the times they were committed to public service, are those the valuations that should be used to include the parcels in the rate base in this case?

A. No. As discussed above, the Guidelines call for recognizing the transactions at the lower of prevailing market price or net book value. The appraisal does not provide the net book value. Goodman has not provided the book value of the parcels as carried by EC Development. The Company knows from Mr. McMurry's direct testimony[17] that Staff is recognizing the Guidelines as the appropriate basis for recording the transactions.

[15] Bourassa rebuttal p. 3 and Company response to Staff data request GTM-7.9.
[16] Company response to Staff data request GTM 4.3.
[17] Gary McMurry direct p. 9.

Accordingly, if EC Development's net book value was higher than the market price, the Company had a strong incentive to provide the book value in its rebuttal testimony to demonstrate that the market price as determined by the appraisal was the appropriate amount for valuing the transaction. The Company's non-disclosure of evidence regarding the net book value of the parcels suggests that the appraised value exceeds the book value; therefore, the appraised value is not the appropriate amount to recognize in rate base for the parcels.

Q. What is Staff's conclusion regarding the valuations for the land parcels?

A. The Guidelines that generally call for recognizing the land transactions at the lower of prevailing market price or net book value are the appropriate basis for recording the transactions. The Company is responsible for supporting the amounts it claims in rate base, and it has not provided the book values needed to properly value the parcel consistent with the Guidelines. The land parcels should not be recognized at the appraised values, and assumed higher values, due to the Company's unwillingness or inability to support the claimed amounts. Ratepayers should not be disadvantage due to the Company's non-disclosure of information or inability to support its proposed valuations.

Accordingly, Staff concludes that the parcels should be recognized at the lower of the market price or net book carrying value by EC Development. Since the Company has not provided the latter, a proper determination of the parcels valuation cannot be made. Staff concludes that the parcels should be excluded from rate base until the Company provides appropriate supporting information. In the meantime, the 2009 Pinal County Assessor's Full Cash Value ("FCV") for the four parcels is a reasonable place holder value. Staff uses the FCV in rate base calculations only to provide a realistic representation of its overall revenue requirement and rates.

Q. What is Staff recommending?

A. Staff recommends valuing the four land parcels at the lower of the market price or net book carrying value by EC Development if and when the Company provides sufficient support for such a determination. As a place holder, Staff is using the 2009 Pinal County Assessor's FCV which results in a $379,837[18] reduction in the land's basis to $114,322, as shown in Surrebuttal Schedule GLF-5. Staff's land value is $344,837 less than the Company's rebuttal value of $459,159.

Rate Base Adjustment No. 2 – Reclassify Water Treatment Plant

Q. What did the Company propose in its initial application with respect to water treatment equipment?

A. Goodman proposed a balance of $15,947 in account number 320, Water Treatment Plant.

Q. Is general account number 320 normally divided into subaccounts?

A. Yes. Normally, account number 320 is divided into subaccounts. Since there is a significant difference in the expected lives of various water treatment equipment, it is appropriate to establish subaccounts, each with its own depreciation rate.

Q. What does Staff recommend with respect to the Water Treatment Equipment?

A. Based on the Company's response to Staff data request GTM-1.5, Staff recommends reclassifying $15,947 to G/L account 320.2, Chemical Solution Feeders, as shown in Surrebuttal Schedule GLF-6. The Company adopts Staff's recommendation in its rebuttal testimony.[19]

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[18] Corrected from $369,500 in Staff's direct testimony.
[19] Bourassa rebuttal, p. 3.

Rate Base Adjustment No. 3 – Reclassify Distribution Reservoirs

Q. What did the Company propose in its initial application with respect to distribution reservoirs?

A. Goodman's application proposes $836,890 in G/L account number 330, Distribution Reservoirs and Standpipe.

Q. Is general account number 330 normally divided into subaccounts?

A. Yes. Similar to the discussion above regarding Water Treatment Equipment, normally, account number 330, Distribution Reservoirs, is divided into subaccounts to recognize the various types of equipment and their respective lives, each with its own depreciation rate.

Q. What is Staff recommending?

A. Staff recommends reclassifying the $836,890 from G/L account number 330, Distribution Reservoirs and Standpipe, to two sub-accounts: $384,827 going to account 330.1, Storage Tanks, and $452,063 going to account 330.2, Pressure Tanks, as shown in Surrebuttal Schedule GLF-7. The Company adopts Staff's recommendation in its rebuttal testimony.[20]

Rate Base Adjustment No. 4 – Reduce Storage Tanks

Q. Does the Company's rebuttal testimony propose to reduce the initial filing amount claimed for storage tanks by $72,350?

A. Yes. The Company witnesses agree that the 190,000 gallon upsize to plant the storage tank at plant no. 3 valued at $72,350 represents excess capacity,[21] and Staff is accepting the Company's rebuttal position. Staff made the $72,350 deduction from the $384,827

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[20] Bourassa rebuttal, p. 3.
[21] Bourassa rebuttal, p. 3; Shiner rebuttal, p.14; Taylor rebuttal, p. 13.

reclassified to account number 330.1, Storage Tanks, as discussed in Staff Rate Base Adjustment No. 3.

Q. What is Staff recommending?

A. Staff recommends an $72,350 negative adjustment to the storage tanks balance, as shown in Surrebuttal Schedule GLF-8. Staff's surrebuttal recommendation for a storage tank balance of $312,477 agrees with the Company's rebuttal balance.

Rate Base *Adjustment* No. 5 – Reduce Transmission and Distribution Mains

Q. What did the Company propose with respect to transmission and distribution mains?

A. In the Company's application, it recorded $1,611,320 in G/L account 331, Transmission and Distribution Mains.

Q. Does Staff have any revision to the $105,564 amount removed from Transmission and Distribution Mains in its direct testimony because of not used and useful plant?

A. Yes. The surrebuttal testimony of Staff witness Marlin Scott, Jr. discusses why an additional $23,036 amount of the transmission mains are not used and useful to the Company's ratepayers. Staff's recommended Transmission and Distribution Mains Value is $105,564 less than the Company rebuttal proposal of $1,611,320.

Q. What is Staff recommending?

A. Staff recommends a decrease of $128,600, as shown in Surrebuttal Schedule GLF-9, to reflect the portion of plant determined to be not used or useful to the production of water service by the Company.

Rate Base Adjustment No. 6 – Reduce Accumulated Depreciation

Q. What did the Company propose with respect to accumulated depreciation?

A. The Company's application proposed $731,205 in accumulated depreciation reflecting a $67,829 pro forma decrease from the end of test year recorded amount of $799,034.

Q. Did the Company's rebuttal testimony propose a modifications to its proposed balance for accumulated depreciation?

A. Yes. The Company's rebuttal testimony increases the accumulated deprecation balance by $2,510 to $733,716 to reflect correction of a computational error and removal of accumulated depreciation on the 190,000 gallon storage tank upsizing that the Company is removing in its rebuttal testimony.[22]

Q. Is Staff making a modification from the $733,602 accumulated depreciation balance in its direct testimony?

A. Yes. Staff is making corrections due to computational errors. In addition, adjustments are necessary to reflect changes in Staff's recommended plant balances. Staff's rebuttal accumulated depreciation balance is $723,295 as shown in Surrebuttal Schedule GLF-10.

Q. What is Staff recommending?

A. Staff recommends decreasing Accumulated Depreciation by $7,910 from $731,205 to $723,295, as shown in Surrebuttal Schedule GLF-10. Staff's surrebuttal recommendation is $10,421 less than the Company's rebuttal proposal of $733,716.

[22] Bourassa rebuttal, p. 3.

Rate Base Adjustment No. 7 – Advances in Aid of Construction

Q. Does Staff have any comment to the Company's assertion that all of the disallowances Staff recommends to Transmission and Distribution Mains were funded with AIAC, and if Staff's adjustment to the transmission and distribution mains is adopted an equal amount of AIAC must also be excluded from rate base?[23]

A. Although the supporting data provided by the Company is insufficiently detailed to show with certainty that the plant Staff recommends be disallowed because it is not used and useful was funded by AIAC, the summary information tends to support that the Company used AIAC funding. The Company's claim that the plant in question was funded by AIAC is further supported by its policy to fund all non-backbone plant with AIAC. The Company's claim that the amount of AIAC excluded from rate base must equal the amount of disallowed plant will be correct only if no there have been no AIAC refunds. Since the plant is not used and useful, it is a reasonable conclusion that there have been no AIAC refunds in recognition that refund obligation are based on revenues generated. Accordingly, Staff concludes that the Company is correct that the disallowance of Transmission and Distribution Mains should be offset by an equal amount of AIAC.

Q. What is Staff recommending?

A. Staff recommends decreasing AIAC by $128,600 from $2,101,905 to $1,973,305, as shown in Surrebuttal Schedule GLF-10.1. Staff's surrebuttal recommendation is $128,600 less than the Company's rebuttal proposal of $2,101,905.

[23] Bourassa rebuttal, pp. 12-14.

Rate Base Adjustment No. 8 – Accumulated Deferred Income Taxes

Q. What did the Company propose with respect to ADIT?

A. The Company's application proposed a $135,342 ADIT credit (reduction to rate base). The entire amount represents a pro forma adjustment to the Company's records at the end of the test year.

Q. Did the Company's rebuttal testimony propose a modifications to its proposed balance for ADIT?

A. Yes. The Company's rebuttal testimony decreases from its direct testimony ADIT by $5,713 to $129,629 to reflect changes to plant, accumulated depreciation and AIAC.[24]

Q. Does Staff have any comments regarding Mr. Bourassa's calculation of ADIT using Staff's direct testimony recommendations and assertion that Staff's ADIT recommendation should be reduced by approximately $47,349 to $87,994 from $135,342?[25]

A. Yes. First, Staff's review of Mr. Bourassa's methodology for calculation of ADIT did not identify any errors that would provide an incorrect ADIT balance assuming use of the correct input values. Second, although Staff did not identify any incorrect input values used in the calculation, it either does not have or could not locate the data necessary to verify the tax basis values used in the calculation. Third, Staff surrebuttal values for plant, accumulated depreciation and AIAC have been modified from its direct testimony rendering the ADIT calculation stale. Fourth, Staff has recalculated the ADIT balance to reflect its surrebuttal balances for plant, accumulated depreciation and AIAC and assuming the tax basis amounts provided in Mr. Bourassa calculations are correct. Staff's calculation results in an ADIT credit balance of $118,506.

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[24] Bourassa rebuttal, p. 30.
[25] Bourassa rebuttal, p. 31.

Q. What is Staff recommending?

A. Staff recommends decreasing the ADIT credit (liability) balance by $16,936 from $135,342 to $118,506, as shown in Surrebuttal Schedule GLF-10.2. Staff's surrebuttal recommendation is $10,821 less than the Company's rebuttal proposal of $129,327.

VIII. OPERATING INCOME

REVENUES

Q. Please summarize the results of Staff's examination of test year operating income.

A. Staff determined a test year operating income of $75,617, $1,735 higher than the adjusted test year operating income of $73,882 in the Company's application, and it is $1,673 higher than the adjusted operating income of $73,944 in the Company's rebuttal testimony. Staff's recommendation results from the operating income adjustments described below.

Operating Income Adjustment No. 1 – Revenue Annualization

Q. What does the Company application propose for operating revenues?

A. The Company's direct testimony proposed the recorded test year revenues of $580,110 less a $7,359 pro forma revenue annualization adjustment for adjusted test year revenues of $572,751.

Q. Does the Company's rebuttal testimony propose modifications to its direct testimony in regard to test year operating revenue?

A. Yes. The Company's rebuttal testimony modifies the annualization adjustment from a $7,359 decrease to a $14,349 increase.[26] The modification results from the Company's

[26] Bourassa rebuttal, p. 35.

discovery that the original bill count did not contain billing determinants for zero usage or reflect pro-rated bills.[27]

Q. Does Staff have comments regarding the Company's modified billing determinants and test year revenue?

A. Yes. The Company's revised annualization adjustment increases its proposed test year revenue by $21,708, from $572,751 to $594,459. Staff is recognizing the revised billing determinants as correct. Staff had rejected the Company initial annualization adjustment because it was inconsistent with trended revenues and customer growth data. The revised annualization is consistent with this data, therefore, Staff is accepting the Company's rebuttal annualization adjustment for test year revenues.

Q. What is Staff recommending?

A. Staff recommends increasing test year revenue by $21,708, from $572,751 to $594,459 through recognition of an annualization adjustment, as shown in Surrebuttal Schedule GLF-13. Staff's surrebuttal recommendation is the same as the Company's rebuttal proposal.

Operating Income Adjustment No. 2 – Rate Case Expense

Q. What did the Company propose for rate case expense in its application?

A. The Company proposed $80,000 amortized over four year, or $20,000 per year.[28]

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[27] Bourassa rebuttal, p. 34.
[28] Bourassa rebuttal, p. 32.

Q. Does the Company's rebuttal testimony propose modifications to its direct testimony in regard to rate case expense?

A. Yes. The Company's rebuttal testimony requests to amortize $160,000 over four years, or $40,000 per year. The Company cite RUCO's intervention, major differences between the parties unlikely to be resolved by the time of the hearing and having already incurred $84,000 prior to its rebuttal filing as reasons for the modification.[29]

Q. Does Staff agree that the Company's increased request for rate case expense is reasonable?

A. Yes. Staff agrees that that $40,000 per year is a reasonable rate case expense. However, Staff recommends recognizing $40,000 per year as the normalized expense, not $160,000 amortized over 4 years. Staff does not support establishing a regulatory asset for rate case expense that may be recovered in subsequent rate cases if not fully recovered in the intervening years.

Q. What is Staff recommending?

A. Staff recommends increasing rate case expense by $20,000, from $20,000 to $40,000, as shown in Surrebutal Schedule GLF-14. Staff's surrebuttal recommendation is the same as the Company's rebuttal proposal in dollar amount, but it is achieve via different accounting and ratemaking treatment as discussed above.

[29] Bourassa rebuttal, p. 33.

Operating Income Adjustment No. 3 – Water Testing Expense

Q. What is the Company proposing for Water Testing Expense?

A. Goodman's application proposes its actual recorded test year amount of $1,215 for water testing.

Q. Is the Company's actual test year water testing expense representative of its average on-going expense?

A. No. Water testing expense varies from one year to the next based on the scheduled intervals for the various tests. Accordingly, water testing expense should be normalized. Staff has determined that the on-going average water testing expense should be $2,783.

Q. Does the Company's rebuttal testimony propose modifications to its direct testimony in regard to test year water testing expense?

A. Yes. The Company's rebuttal testimony adopts Staff's $1,568 adjustment to increase water testing expense to $2,783.

Q. What is Staff recommending?

A. Staff recommends Water Testing expense of $2,783, a $1,568 increase from the Company's reclassified amount as shown in Surrebuttal Schedule GLF-15. Staff's surrebuttal recommendation is the same as the Company's rebuttal proposal.

Operating Income Adjustment No. 4 – Depreciation Expense

Q. What did the Company propose for Depreciation expense in its application?

A. The Company proposed its recorded test year depreciation expense of $228,578 less a $723 pro forma adjustment for $227,855.

Q. Does the Company's rebuttal testimony propose modifications to its direct testimony in regard to depreciation testing expense?

A. Yes. The Company's rebuttal testimony increases the proposed depreciation expense by $13,619 over the $227,855 amount requested in its filing to $241,474 due to changes in plant values.

Q. Has Staff also revised its recommended depreciation expense?

A. Yes. As shown in Surrebuttal Schedule GLF-16, Staff recalculated depreciation expense by applying Staff's recommended depreciation rates to Staff's recommended plant by account. Staff calculated depreciation expense of $238,902, an increase of $11,047 from the $227,855 proposed by the Company in its application due to changes in recommended plant values.

Q. What is Staff recommending?

A. Staff recommends $238,902 for Depreciation expense, an $11,047 increase from the amount proposed in the Company's application, as shown in Surrebuttal Schedule GLF-16. Staff's surrebuttal recommendation is $2,572 less than the Company's rebuttal proposal of $241,474.

Operating Income Adjustment No. 5 – Property Tax Expense

Q. What did the Company propose in its application for test year property tax expense?

A. Goodman proposed $21,299 for test year property taxes. The proposed amount is $12,722 greater than the $8,576 recorded in the test year. The Company calculated its proposed amount using a modified version of the Arizona Department of Revenue's ("ADOR") property tax method.

Q. What method has the Commission typically adopted to determine property tax expense for ratemaking purposes of Class B water utilities?

A. The Commission's practice in recent years has been to use a modified ADOR methodology for water and wastewater utilities.

Q. Using the modified ADOR property tax method, what is the primary factor for determining the amount of property tax calculated?

A. The results from the modified ADOR methodology are primarily dependent upon revenue inputs for three years. In the same manner as each operating income has a specific income tax expense, there is a specific property tax expense for each three-year set of revenue inputs. Therefore, the property tax expense calculated for the test year is different than the property tax calculated for the authorized revenue. Only when the revenue inputs for all three years is equal to the test year revenue will the resulting calculation reflect property tax expense that correlates with the test year revenue. Since under the modified ADOR method property tax expense is revenue-dependent in the same manner as is income tax expense, property tax expense must be recalculated to reflect the authorized revenue. Using inputs of one year of authorized revenue and two years of test year revenue in the modified ADOR method provides the average expected property tax over a subsequent three-year period. Use of one year of authorized revenue and two years of test year revenue is consistent with the tax assessment lags used by ADOR.

Q. What revenues did the Company use to calculate test year property tax expense?

A. Schedule C-2, page 3, of the Company's application shows that it used one year of proposed revenue and two years of test year revenues to calculate test year property tax expense.

Q. Did the Company's property tax calculations as proposed in its application reflect an appropriate amount for test year property tax expense?

A. No. As discussed above, only when the revenue input for all three years is equal to the test year revenue will the resulting calculation using the modified ADOR method reflect property taxes that correlate with test year revenue. Since the Company included one year of proposed revenue in its calculation, its proposed test year property tax expense reflects the on-going property tax expense, as opposed to test year expense, and will only reflect the on-going expense if the Company's proposed revenue is adopted.

Q. Has Staff developed a solution to address the dependent relationship between Property Tax expense and revenues?

A. Yes. Staff has included a factor for property taxes in the gross revenue conversion factor ("GRCF") (see Surrebuttal Schedule GLF-2) that automatically adjusts the revenue requirement for changes in revenue in the same way that income taxes are adjusted for changes in operating income. This flexible method will accurately reflect property tax expense at any authorized revenue level. This refinement allows for accurate calculation of property tax expense at the test year revenue level, and for recovery of any additional property tax expense incurred due to any increase in authorized revenue. It also removes any necessity to present on-going property tax expense as test year property tax expense. In using the GRCF to calculate the correct revenue requirement, the test year operating income must be determined with property tax expense derived from the modified ADOR method using test year revenue as the input for all three years.

Q. Does the Company's rebuttal testimony propose modifications to its direct testimony in regard to property tax expense?

A. Yes. The Company's rebuttal testimony adopts the modified ADOR method used by Staff. Accordingly, the difference between Staff's surrebuttal and the Company's rebuttal property tax expense is primarily due to differences in revenue.

Q. What is Staff's surrebuttal recommendation for test year property tax expense?

A. Staff recommends $19,049 for test year property tax expense, a $2,250 reduction from the Company's proposed amount of $21,299, as shown in Surrebuttal Schedule GLF-17.[30] Staff further recommends adoption of its GRCF that includes a factor for property tax expense, as shown in Surrebuttal Schedule GLF-2. Staff's surrebuttal recommendation is $886 less than the Company's rebuttal proposal of $19,935.

Operating Income Adjustment No. 6 – Income Tax Expense

Q. What did the Company propose in its application for test year income tax expense?

A. Goodman proposed $22,873 for test year income tax expense in its application. The Company's test year income tax expense reflects application of the statutory State and Federal income tax rates to its adjusted test year income.

Q. Does the Company's rebuttal testimony propose a change to its direct testimony in the amount of income tax expense to reflect changes in revenue and expenses in its rebuttal testimony?

A. Yes. The Company's rebuttal testimony proposes test year income tax expense of $10,120.[31]

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[30] Schedule GLF-11 also shows calculations for Property Tax Expense for Staff's recommended revenue.
[31] Bourassa Rebuttal Schedule C-2, , p. 7.

Q. Did Staff also update its recommended test year income tax expense to reflect changes in revenues and expenses in its surrebuttal testimony?

A. Yes. Staff calculated test year income tax expense of $11,904 by applying the statutory State and Federal income tax rates to Staff's adjusted test year taxable income, as shown in Surrebuttal Schedule GLF-2.

Q. Since Staff and the Company used the same tax rates and methods to calculate test year income tax expense, what accounts for the difference between the Staff and the Company test year income tax expenses?

A. Staff and the Company used different test year operating expenses and synchronized interest to calculate taxable income.

Q. What is Staff recommending?

A. Staff recommends reducing test year income tax expense by $10,969, from $22,873 to $11,904, as shown in Surrebuttal Schedules GLF-2 and GLF-18. Staff's surrebuttal recommendation is $1,784 greater than the Company's rebuttal proposal of $10,250.

Q. Does Staff have any additional comments regarding income taxes?

A. Yes. On Rebuttal Schedule C-3, the Company shows its calculation of a 1.7130 gross revenue conversion factor. Surrebuttal Schedule GLF-2 shows the calculation of Staff's 1.7049 GRCF. Staff Surrebuttal Schedule GLF-2 provides a reconciliation of Staff's test year and recommended revenues. The reconciliation shows the incremental operating income, property tax expense and income tax expense components of Staff recommended increase in revenue. The reconciliation verifies that Staff's 1.7049 GRCF results in the recommended operating income.

Operating Income Adjustment No. 7 – Annualize Purchased Power Expense

Q. What did the Company propose in its application for purchased power expense?

A. Goodman proposed its recorded test year amount of $27,066 for purchased power expense in its application.

Q. Does the Company's rebuttal testimony propose modifications to its direct testimony in regard to purchased power testing expense?

A. Yes. The Company's rebuttal testimony proposes an annualization adjustment that increases purchased power expense by $577 to $27,642 to recognize the additional cost to pump water due to its annualization of test year revenues.[32]

Q. Is Staff in agreement with the Company's annualization adjustment for purchased power?

A. Yes. This annualization adjustment is consistent with Staff's annualization of test year revenues.

Q. What is Staff recommending?

A. Staff recommends increasing purchased power expense by $577, from $27,066 to $27,642, as shown in Surrebuttal Schedule GLF-18.1. Staff's surrebuttal recommendation is the same as the Company's rebuttal proposal.

[32] Bourassa Rebuttal Schedule C-2, p. 7.

IX. AFFILIATED TRANSACTIONS

Q. Does Staff have any comments regarding affiliate transactions in response to the Company's rebuttal testimony?

A. Only as stated in other sections of this testimony. E.g., in response to Mr. Shiner's rebuttal, Staff notes that it continues to advocate that the Company develop and implement written policies to guide the Company in affiliated transactions and hiring of outside consultants.

X. RATE DESIGN

Q. Does Staff have any comments regarding rate design in response to the Company's rebuttal testimony?

A. As noted by the Company, the Staff and Company rate structures are similar with the same break-over points, similar percentages of revenue recovered through the monthly minimum charges and the commodity rates.[33] Although the differences are minor, the percentages of revenue statistics used in page 42 of Mr. Bourassa's rebuttal are in error due to an incorrect formulaic cell reference in the document – Exhibit, Page 3, Goodman Water Company – Staff Proof, Revenue Breakdown Summary, Metered Revenues – Staff Proposed Rates. Also, Staff notes that the rate design presented on pages 39 and 40 of Mr. Bourassa's testimony are inconsistent with his Rebuttal Schedule H-3 with the latter being the actual rates used in his calculation of revenues.

Staff also notes that the Company's rebuttal testimony adopts Staff's recommendations for all miscellaneous charges including after-hours charges and elimination of the turn on/off charge.[34]

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[33] Bourassa rebuttal, p. 42.
[34] Bourassa rebuttal, p. 44.

Staff's Recommended Water Rate Design

Q. Please provide a description of Staff's surrebuttal recommended rate structure for the water system.

A. Staff recommends continuation of the fundamental existing rate structure. Staff recommends the following monthly fixed charges by customer class: 5/8 x 3/4-inch meter, $51.00; 3/4-inch meter, $76.50; 1-inch meter, $128.00; 1.5-inch meter, $255.00; 2-inch meter, $408.00; 3-inch meter, $816.00; 4-inch meter, $1,275.00; and 6-inch meter, $2,550.00. Staff recommends the following commodity rates per 1,000 gallons of water use by the 5/8 x 3/4-inch residential class, 1 to 3,000 gallons, $4.80 per 1,000 gallons; 3,001 to 9,000 gallons, $9.75 per 1,000 gallons; and over 9,000 gallons, $11.75 per 1,000 gallons.

Q. Did Staff prepare schedules showing the present, Company proposed, and Staff recommended monthly minimums and commodity rates for each rate class?

A. Yes. Staff's Surrebuttal Schedule GLF-19 shows the present monthly fixed charges and commodity rates, the Company's proposed monthly fixed charges and commodity rates and Staff's recommended monthly fixed charges and commodity rates.

Q. Did Staff prepare a schedule showing the average and median monthly bill under present rates, the Company's proposed rates, and Staff's recommended rates?

A. Yes. Staff's Surrebuttal Schedule GLF-20 presents the typical bill analysis for a residential water customer using present rates, the Company's proposed rates and Staff's recommended rates.

Q. What is the impact to the median customer bill with Staff's rate design?

A. Staff's recommended rates would increase the typical residential water bill with median month usage of 4,500 gallons by $19.07, or 31.29 percent, from $60.96 to $80.03.

Q. Will Staff's recommended rate design generate Staff's surrebuttal revenue requirement?

A. Staff's recommended rate design would generate Staff's recommended water revenue requirement of $775,283, composed of $761,545 from water sales and $13,738 from other revenues.

XI. STAFF'S RESPONSE TO THE REBUTTAL TESTIMONY OF THOMAS J. BOURASSA

Q. Does Staff have any comment on Mr. Bourassa's assertion that the statement on page 10 of Mr. McMurray's direct testimony that Mr. Naifeh had a two percent interest in D&D Investments West, LLC is inaccurate?

A. Yes. Staff retracts the question and answer in Mr. McMurry's testimony on page 10, line 1-3. The relationship between Mr. Naifeh and Mr. Sears that results in Mr. Naifeh's lack of independence is described in Mr. Naifeh's rebuttal testimony at pages 7 and 8, and it is summarized above under Rate Base Adjustment No. 1 – Reduce Cost Basis for Land Purchase.

Q. Does Staff have any comment on Mr. Bourassa's assertion that the Commission should authorize an accounting order relating to deferred depreciation expense for future recovery if either Staff or RUCO recommended disallowances for excess capacity are adopted?[35]

A Yes. The Commission should deny the Company's request for an accounting order to defer depreciation expense on any plant the Commission excludes from rate base that represents excess capacity. Such authorization would effectively provide impunity to the Company for building excess capacity by providing an opportunity for future recovery of plant that never benefitted ratepayers. Depreciation expense represents an allocation of the cost of plant over its tangible life. The portion of the life that expires while the plant is excess capacity cannot be recaptured at a future date, and therefore, cannot provide benefits to ratepayers at a future date. Depreciation expense incurred on plant deemed excess capacity should be borne by shareholders, not ratepayers.

XII. STAFF'S RESPONSE TO THE REBUTTAL TESTIMONY OF JAMES A. SHINER

Q. Do you have any response to Mr. Shiner's rebuttal testimony?

A. Yes. First, Mr. Shiner's rebuttal testimony presents a general discussion regarding valuation of the land parcels, excess storage capacity and rate case expense. These issues are addressed above under Rate Base Adjustment No. 1 – Reduce Cost Basis for Land Purchase, Rate Base Adjustment No. 4 – Excess Capacity – Storage Tank, and Operating Income Adjustment No. 2 – Rate Case Expense.

Next, Mr. Shiner states that the Company is willing to develop and implement written policies of the type (affiliated transactions and hiring of outside consultants) recommended by Mr. McMurry if the Commission determines they are necessary.[36] Staff

[35] Bourassa rebuttal, p. 29.
[36] Shiner rebuttal, p. 20.

continues to advocate that the Company develop and implement written policies to guide the Company for these types of transactions. Written policies provide multiple benefits including an opportunity to evaluate and improve existing practices, operating efficiency, consistency and continuity.

XIII. STAFF'S RESPONSE TO THE REBUTTAL TESTIMONY OF MARK TAYLOR

Q. Do you have any response to Mr. Taylor's rebuttal testimony?

A. No. The issues addressed in Mr. Taylor's rebuttal testimony pertain to issues outside the scope of my testimony, and those issues are addressed in the testimonies of other Staff witnesses.

XIV. STAFF'S RESPONSE TO THE REBUTTAL TESTIMONY OF MICHAEL J. NAIFEH

Q. Does Staff have any comments regarding Mr. Naifeh's rebuttal testimony other than those discussed above under Rate Base Adjustment No. 1 – Reduce Cost Basis for Land Purchase?

A. Yes. First, Mr. Naifeh expressed concern that Mr. McMurry's direct testimony claims his 2008 appraisal was flawed.[37] Mr. McMurry's testimony identifies four reasons to question the value that the Company used to record the land including the unintended statement, "Fourth, the appraisal was flaw."[38] Staff retracts that portion of Mr. McMurry's direct testimony, and apologizes for this oversight.

Mr., Naifeh also expressed concern that Mr. McMurry's direct testimony at page 10, line 9 cites Federal Deposit Insurance Corporation regulations and requirements for appraisers,

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[37] Naifeh rebuttal, p. 11.
[38] McMurry direct, p. 8.

and he claims that those regulations are not applicable. Staff is retracting following language from Mr. McMurry's testimony.

> There are both appraisal guidelines and Federal Deposit Insurance Corporation regulations that require that an appraiser have not interest, financial or otherwise, in the property or the transaction.

XV. STAFF'S RESPONSE TO THE REBUTTAL TESTIMONY OF JOHN FERENCHAK III

Q. Does Staff have any comments regarding Mr. Ferenchak III's rebuttal testimony?

A. Yes. Most of Staff's comments pertaining to Mr. Ferenchak III's rebuttal testimony are addressed above under Rate Base Adjustment No. 1 – Reduce Cost Basis for Land Purchase. That testimony notes that Staff used the 2009 Pinal County Assessor's FCV for the four parcels is a reasonable place holder value. Mr. Ferenchak III's identifies the tax parcel numbers for those four parcels and there respective 2010 FCVs as follows: Water Plant #1 – Ptn of 305-31-013W ($223,680); Water Plant #2 – 305-31-013Q ($46,874); Water Plant #3 – 305-93-6040 ($500); and Water Plant #4 – 30593-219B ($28,000).[39] Staff's direct testimony Schedule GTM-5 used a different parcel number for water plant no. 1 and transcribed the parcel numbers for water plant nos. 3 and 4. Surrebuttal Schedule GLF-5 corrects the transcription and uses the same parcel number (305-31-013W) for water plant no. 1 as does Mr. Ferenchak III.

Also, as Mr. Ferenchak III notes in the tables in the executive summary of his appraisal, dated April 29, 2011, only 31,363 square feet (0.72 acres) of the 9.32 acre parcel is dedicated to water plant no. 1. Accordingly, Staff assigned a pro-rata portion [(0.72 ÷

[39] Ferenchak III rebuttal, Attachment A, p.16.

9.32) x $28,000 = $2,163] of the FCV to that parcel. Further, although the 2009 FCV for Water Plant #3 – 305-93-6040 is $500, Staff used the higher value ($28,000) pertaining only to the land.

XVI. STAFF'S RESPONSE TO THE REBUTTAL TESTIMONY OF JAMES SCHOEMPERLEN

Q. Do you have any response to Mr. Schoemperlen's rebuttal testimony?

A. Yes. Although the issues addressed in Mr. Schoemperlen's rebuttal testimony pertain to issues generally outside the scope of my testimony, and those issues are addressed in the testimonies of other Staff witnesses, in his discussions of these issues he discusses an accounting/ratemaking concept. Specifically, Mr. Schoemperlen projects that since the mix of fixed and variable costs do not remain constant with customer/revenue growth, recognizing the plant values for capacity in excess of test year customers will result in growth in returns.[40] Mr. Schoemperlen's observation is correct. However, the regulatory framework recognizes this benefit to utilities. The regulatory framework has both regulatory benefits and liabilities. Utilities are quick to draw attention to the liabilities and ignore the benefits. The regulator's responsibility is to find an optimal balance between the benefits and liabilities, not necessarily to eliminate them.

[40] Schoemperlen rebuttal p. 8.

XVII. STAFF'S RESPONSE TO THE REBUTTAL TESTIMONY OF LAWRENCE WAWRZYNIAK

Q. What is Staff's response to Mr. Wawrzyniak's concern that Staff under reports the number of customer opinions/complaints received because petitions signed by multiple customers are counted as a single opinion/complaint?

A. Yes. Staff has revised its reported statistical data to opinions and complaints. Mr. Wawrzyniak's testimony provides a summary of opinions and complaints filed with the Commission. This appears to be raw data. Staff has found individuals and households sometimes file multiple communications, and Staff's reported communications reflect removal of multiple opinions and complaints from a single individual or household. Accordingly, Staff's reported statistics will not agree with the raw data.

Q. Does this conclude your Surrebuttal Testimony?

A. Yes, it does.

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SURREBUTTAL TESTIMONY - GORDON L. FOX

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Surrebuttal Schedule GLF-1

REVENUE REQUIREMENT

LINE NO.	DESCRIPTION		(A) COMPANY ORIGINAL COST		(B) COMPANY FAIR VALUE		(C) STAFF ORIGINAL COST		(D) STAFF FAIR VALUE
1	Adjusted Rate Base	$	2,402,222	$	2,402,222	$	1,974,781	$	1,974,781
2	Adjusted Operating Income (Loss)	$	73,882	$	73,882	$	75,617	$	75,617
3	Current Rate of Return (L2 / L1)		3.08%		3.08%		3.83%		3.83%
4	Required Rate of Return		10.54%		10.54%		9.20%		9.20%
5	Required Operating Income (L4 * L1)	$	253,194	$	253,194	$	181,680	$	181,680
6	Operating Income Deficiency (L5 - L2)	$	179,312	$	179,312	$	106,063	$	106,063
7	Gross Revenue Conversion Factor		1.6254		1.6254		1.7049		1.7049
8	Required Revenue Increase (L7 * L6)	$	291,454	$	291,454	**$**	**180,824**	**$**	**180,824**
9	Adjusted Test Year Revenue	$	572,751	$	572,751	$	594,459	$	594,459
10	Proposed Annual Revenue (L8 + L9)	$	864,205	$	864,205	$	775,283	$	775,283
11	Required Increase in Revenue (%)		50.89%		50.89%		30.42%		30.42%
12	Rate of Return on Common Equity (%)		11.00%		11.00%		9.10%		9.10%

References:
Column (A): Company Schedule B-1
Column (B): Company Schedule B-1
Column (C): Company Schedules A-1, A-2, & D-1
Column (D): Staff Schedule GLF-2 , GLF-3 & GLF-11

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GROSS REVENUE CONVERSION FACTOR

LINE NO.	DESCRIPTION	(A)	(B)	(C)	(D)
	Calculation of Gross Revenue Conversion Factor:				
1	Revenue	100.0000%			
2	Uncollecible Factor (Line 11)	0.0000%			
3	Revenues (L1 - L2)	100.0000%			
4	Combined Federal and State Tax Rate (Line 17) + Property Tax Factor (Line 23)	41.3448%			
5	Subtotal (L3 - L4)	58.6552%			
6	**Revenue Conversion Factor (L1 / L5)**	1.7049			
	Calculation of Uncollectible Factor:				
7	Unity	100.0000%			
8	Combined Federal and State Tax Rate (Line 17)	40.7558%			
9	One Minus Combined Income Tax Rate (L7 - L8)	59.2442%			
10	Uncollectible Rate	0.0000%			
11	Uncollectible Factor (L9 * L10)	0			
	Calculation of Effective Tax Rate:				
12	Operating Income Before Taxes (Arizona Taxable Income)	100.0000%			
13	Arizona State Income Tax Rate	6.9680%			
14	Federal Taxable Income (L12 - L13)	93.0320%			
15	Applicable Federal Income Tax Rate (Line 53)	36.3185%			
16	Effective Federal Income Tax Rate (L14 x L15)	0.33787801			
17	Combined Federal and State Income Tax Rate (L13 +L16)	40.7558%			
	Calculation of Effective Property Tax Factor				
18	Unity	100.0000%			
19	Combined Federal and State Tax Rate (Line 17)	40.7558%			
20	One Minus Combined Income Tax Rate (L18 - L19)	59.2442%			
21	Property Tax Factor (GLF-17, L26)	0.9941%			
22	Effective Property Tax Factor (L 21 * L 22)	0.5890%			
23	Combined Federal and State Tax and Property Tax Rate (L17+L22)		41.3448%		
24	Required Operating Income (Schedule GLF-1, Line 5)	$ 181,680			
25	AdjustedTest Year Operating Income (Loss) (Schedule GLF-11, Line 33)	$ 75,617			
26	Required Increase in Operating Income (L24 - L25)		$ 106,063		
27	Income Taxes on Recommended Revenue (Col. (D), L52)	$ 84,867			
28	Income Taxes on Test Year Revenue (Col. (B), L52)	$ 11,904			
29	Required Increase in Revenue to Provide for Income Taxes (L27 - L28)		$ 72,964		
30	Recommended Revenue Requirement (Schedule GLF-1, Line 10)	$ 775,283			
31	Uncollectible Rate (Line 10)	0.0000%			
32	Uncollectible Expense on Recommended Revenue (L24 * L25)	$ -			
33	Adjusted Test Year Uncollectible Expense	$ -			
34	Required Increase in Revenue to Provide for Uncollectible Exp. (L32 - L33)		$ -		
35	Property Tax with Recommended Revenue (GLF-17, L21)	$ 20,846			
36	Property Tax on Test Year Revenue (GLF-17, L22)	$ 19,049			
37	Increasee in Property Tax Due to Increase in Revenue (GLF-17, L23)		$ 1,798		
38	Total Required Increase in Revenue (L26 + L29 + L34+L37)		$ 180,824		
	Calculation of Income Tax:	Test Year		STAFF Recommended	
39	Revenue (Schedule GLF-11, Col.[C], Line 5 & Sch. GLF-1, Col. [D], Line 10)	$ 594,459		$ 775,283	
40	Operating Expenses Excluding Income Taxes	$ 506,938		$ 508,736	
41	Synchronized Interest (L56)	$ 31,596		$ 31,596	
42	Arizona Taxable Income (L39 - L40- L41)	$ 55,924		$ 234,951	
43	Arizona State Income Tax Rate	6.9680%		6.9680%	
44	Arizona Income Tax (L42 x L43)		$ 3,897		$ 16,371
45	Federal Taxable Income (L42 - L44)	$ 52,028		$ 218,579	
46	Federal Tax on First Income Bracket ($1 - $50,000) @ 15%	$ 7,500		$ 7,500	
47	Federal Tax on Second Income Bracket ($50,001 - $75,000) @ 25%	$ 507		$ 6,250	
48	Federal Tax on Third Income Bracket ($75,001 - $100,000) @ 34%	$ -		$ 8,500	
49	Federal Tax on Fourth Income Bracket ($100,001 - $335,000) @ 39%	$ -		$ 46,246	
50	Federal Tax on Fifth Income Bracket ($335,001 -$10,000,000) @ 34%	$ -		$ -	
51	Total Federal Income Tax		$ 8,007		$ 68,496
52	Combined Federal and State Income Tax (L44 + L51)		$ 11,904		$ 84,867
53	Applicable Federal Income Tax Rate [Col. (D), L51 - Col. (B), L51] / [Col. (C), L44 - Col. (A), L44]				36.32%
	Calculation of Interest Synchronization:				
54	Rate Base (Schedule GLF-3, Col. [C], Line (14))	$ 1,974,781			
55	Weighted Average Cost of Debt (Surrebuttal Schedule JCM-1)	1.60%			
56	Synchronized Interest (L54 X L55)	$ 31,596			

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Surrebuttal Schedule GLF-3

RATE BASE - ORIGINAL COST

LINE NO.		(A) COMPANY AS FILED	(B) STAFF ADJUSTMENTS	REF	(C) STAFF AS ADJUSTED
1	Plant in Service	$ 5,453,761	$ (580,787)		$ 4,872,974
2	Less: Accumulated Depreciation	731,205	(7,910)		723,295
3	Net Plant in Service	$ 4,722,556	$ (572,877)		$ 4,149,679
	LESS:				
4	Contributions in Aid of Construction (CIAC)	$ -	$ -		$ -
5	Less: Accumulated Amortization	-	-		-
6	Net CIAC	$ -	$ -		$ -
7	Advances in Aid of Construction (AIAC)	2,101,905	(128,600)		1,973,305
8	Service Line & Mete Installation Charges	83,087	-		83,087
9	Deferred Income Tax Credits	135,342	(16,836)		118,506
	ADD:				
10	Unamortized Finance Charges	-	-		-
11	Deferred Tax Assets	-	-		-
12	Working Capital	-	-		-
13	Intentionally Left Blank	-	-		-
14	**Original Cost Rate Base**	$ 2,402,222	$ (427,441)		$ 1,974,781

References:
Column (A), Company Schedule B-1
Column [B]: Column [C] - Column [A]
Column [C], GLF-4

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SUMMARY OF ORIGINAL COST RATE BASE ADJUSTMENTS

LINE NO.	ACCT. NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] LAND ADJ #1	[C] WATER TREATMENT ADJ #2	[D] DISTRIBUTION RESERVOIR ADJ #3	[E] DISTRIBUTION RESERVOIR ADJ #4	[F] TRANSMISSION MAINS ADJ #5	[G] ACCUMULATED DEPRECIATION ADJ #6	[C] AIAC ADJ #7	[I] ADIT ADJ #8	[J] STAFF ADJUSTED
	PLANT IN SERVICE:											
1	301	Organization Cost	$ 127,103	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ 127,103
2	302	Franchise Cost	-	-	-	-	-	-	-	-	-	-
3	303	Land and Land Rights	494,159	(379,837)	-	-	-	-	-	-	-	114,322
4	304	Structures and Improvements	182,570	-	-	-	-	-	-	-	-	182,570
5	305	Collecting and Impounding Res.	-	-	-	-	-	-	-	-	-	
6	306	Lake River and other Intakes	-	-	-	-	-	-	-	-	-	-
7	307	Wells and Springs	386,591	-	-	-	-	-	-	-	-	386,591
8	308	Infiltration Galleries and Tunnels	-	-	-	-	-	-	-	-	-	-
9	309	Supply Mains	-	-	-	-	-	-	-	-	-	-
10	310	Power Generation Equipment	-	-	-	-	-	-	-	-	-	-
11	311	Electrical Pumping Equipment	968,652	-	-	-	-	-	-	-	-	968,652
12	320	Water Treatment Equipment	15,947	-	(15,947)	-	-	-	-	-	-	-
13	320.1	Water Treatment Plant		-	-	-	-	-	-	-	-	-
14	320.2	Chemical Solution Feeders		-	15,947	-	-	-	-	-	-	15,947
15	330	Distribution Reservoirs & Standpipe	836,890	-	-	(836,890)	-	-	-	-	-	-
16	330.1	Storage Tanks	-	-	-	384,827	(72,350)	-	-	-	-	312,477
17	330.2	Pressure Tanks	-	-	-	452,063	-	-	-	-	-	452,063
18	331	Transmission and Distribution Mains	1,611,320	-	-	-	-	(128,600)	-	-	-	1,482,720
19	333	Services	386,947	-	-	-	-	-	-	-	-	386,947
20	334	Meters	94,263	-	-	-	-	-	-	-	-	94,263
21	335	Hydrants	161,737	-	-	-	-	-	-	-	-	161,737
22	336	Backflow Prevention Devices	-	-	-	-	-	-	-	-	-	-
23	339	Other Plant & Miscellaneous Equipment	187,582	-	-	-	-	-	-	-	-	187,582
24	340	Office Furniture & Fixtures	-	-	-	-	-	-	-	-	-	-
25	340.1	Computers & Software	-	-	-	-	-	-	-	-	-	-
26	341	Transportation Equipment	-	-	-	-	-	-	-	-	-	-
27	342	Stores Equipment	-	-	-	-	-	-	-	-	-	-
28	343	Tools and Work Equipment	-	-	-	-	-	-	-	-	-	-
29	344	Laboratory Equipment	-	-	-	-	-	-	-	-	-	-
30	345	Power Operated Equipment	-	-	-	-	-	-	-	-	-	-
31	346	Communications Equipment	-	-	-	-	-	-	-	-	-	-
32	347	Miscellaneous Equipment	-	-	-	-	-	-	-	-	-	-
33	348	Other Tangible Plant	-	-	-	-	-	-	-	-	-	-
		Rounding Amount	-	-	-	-	-	-	-	-	-	-
34		Subtotal Plant in Service	$ 5,453,761	$ (379,837)	$ -	$ -	$ (72,350)	$ (128,600)	$ -	$ -	$ -	$ 4,872,974
35												
36	Add:											
37	Other 1	Intentionally Left Blank	-		-	-	-	-	-	-	-	-
38	Other 2	Intentionally Left Blank	-	-		-	-	-	-	-	-	-
39	Less:											
40	Other 3	Intentionally Left Blank	-	-	-	-	-	-	-	-	-	-
41	Other 4	Intentionally Left Blank	-	-	-	-	-	-	-	-	-	-
42												
43	Total Plant in Service:		$ 5,453,761	$ (379,837)	$ -	$ -	$ (72,350)	$ (128,600)	$ -	$ -	$ -	$ 4,872,974
44	Less: Accumulated Depreciation		731,205		-	-	-	-	(7,910)	-	-	$ 723,295
45		Intentionally Left Blank	-	-	-	-	-	-	-	-	-	-
46	Net Plant in Service (L59 - L 60)		$ 4,722,556	$ (379,837)	$ -	$ -	$ (72,350)	$ (128,600)	$ 7,910	$ -	$ -	$ 4,149,679
47												
48	*LESS:*											
49	Contributions in Aid of Construction (CIAC)		$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	-
50	Less: Accumulated Amortization		-	-	-	-	-	-	-	-	-	-
51	Net CIAC (L49 - L50)		$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	-
52	Advances in Aid of Construction (AIAC)		2,101,905	-	-	-	-	-	-	(128,600)	-	1,973,305
53	Service Line & Mete Installation Charges		83,087	-	-	-	-	-	-	-	-	83,087
54	Deferred Income Tax Credit		135,342		-	-	-	-	-	-	(16,836)	118,506
55												
56	*ADD:*											
57	Unamortized Finance Charges		-	-	-	-	-	-	-	-	-	-
58	Deferred Tax Assets		-	-	-	-	-	-	-	-	-	-
59	Working Capital		-	-	-	-	-	-	-	-	-	-
60	Regulatory Asset (Liability)			-	-	-	-	-	-	-	-	-
61	**Original Cost Rate Base**		$ 2,402,222	$ (379,837)	$ -	$ -	$ (72,350)	$ (128,600)	$ 7,910	$ 128,600	$ 16,836	$ 1,974,781

References:
Column [A] Schedule B-2, E-1

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Surrebuttal Schedule GLF-5

ORIGINAL COST RATE BASE ADJUSTMENT # 1 - REDUCE COST BASIS FOR LAND PURCHASE

Line No.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1	303	Land and Land Rights	$ 494,159	$ (379,837)	$ 114,322

Line No.	Accessor's Parcel No.	Acres	Full Cash Value 2009 [1]	Market Value Opinion [2]
2				
3	305-31-013 W (Plant No. 1)	0.72	$ 2,163 [4]	$ 180,000 [3]
5	305-31-013 Q (Plant No. 2)	0.25	40,000	60,000
6	305-93-6040 (Plant No. 3)	0.63	40,000	150,000
7	305-93-219 B (Plant No. 4)	0.39	28,000	100,000
8				
9		1.99	$ 110,163	$ 490,000

(1) - This is the full cash value (FCV) for 2009 as obtained from the Pinal County Assessor's website.
(2) - The Company provided a six page "A Summary Appraisal Report developing market value opinions of the underlying land (a fractional interest appraisal)" by M. Naifeh, MAI, CRE.
(3) - Parcel "one" is comprised of two real estate parcels.
(4) - 0.72 acres / 9.32 acres x $28,000 = $2,163

Staff's basis for Land	
Assesor's FCV - Plant No. 1 calculated	$ 110,163
Closing Costs	2,159
Appraisal Fee	2,000
	$ 114,322

References:
Col [A]: Company Schedule B-1
Col [B]: GLF Testimony
Col [C]: Col. [A] + Col. [B]

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Surrebuttal Schedule GLF-6

ORIGINAL COST RATE BASE ADJUSTMENT # 2 - RECLASSIFY WATER TREATMENT EQUIPMENT

LINE NO.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1	320	Water Treatment Equipment	$ 15,947	$ (15,947)	$ -
2	320.1	Water Treatment Plant		-	-
3	320.2	Chemical Solution Feeders		$ 15,947	$ 15,947
4		Total	$ 15,947	$ -	$ 15,947

References:
Col [A]: Company Schedule B-1
Col [B]: GLF Testimony , SDR GTM-1.5
Col [C]: Col. [A] + Col. [B]

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Surrebuttal Schedule GLF-7

ORIGINAL COST RATE BASE ADJUSTMENT # 3 - RECLASSIFY DISTRIBUTION RESERVOIRS

LINE NO.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1	330	Distribution Reservoirs & Standpipe	$ 836,890	$ (836,890)	$ -
2	330.1	Storage Tanks		$ 384,827	$ 384,827
3	330.2	Pressure Tanks		$ 452,063	$ 452,063
4		Total	$ 836,890	$ -	$ 836,890

References:
Col [A]: Company Schedule B-1
Col [B]: GLF Testimony, SDR GTM-1.4
Col [C]: Col. [A] + Col. [B]

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Surrebuttal Schedule GLF-8

ORIGINAL COST RATE BASE ADJUSTMENT # 4 - ELIMINATE EXCESS CAPACITY - STORAGE TANK

LINE NO.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1	331	Storage Tanks[1]	$ 384,827	$ (72,350)	$ 312,477

[1] The Company proposed amount is the portion claimed by the Company and reclassified by Staff to Acct. 330.1 as shown in GTM-7.

References:
Col [A]: Company Schedule B-1
Col [B]: GLF and MSJ Testimony
Col [C]: Col. [A] + Col. [B]

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Surrebuttal Schedule GLF-9

ORIGINAL COST RATE BASE ADJUSTMENT # 5 - ELIMINATE EXCESS CAPACITY - DISTRIBUTION MAINS

LINE NO.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1	333	Transmission and Distribution Mains	1,611,320	$ (128,600)	$ 1,482,720

References:
Col [A]: Company Schedule B-1
Col [B]: GTM and MSJ Testimony
Col [C]: Col. [A] + Col. [B]

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Surrebuttal Schedule GLF-10

ORIGINAL COST RATE BASE ADJUSTMENT # 6 - ADJUST ACCUMULATED DEPRECIATION

LINE NO.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1		Accumulated Depreciation	$ 731,205	$ (7,910)	$ 723,295
			Accumulated Depreciation per application	Accumulated Depreciation per Staff	Difference
2		Structures and Improvements	$ 10,285	$ 10,285	$ 0
3		Collecting and Impounding Res.	-	-	-
4		Lake River and other Intakes	-	-	-
5		Wells and Springs	67,423	67,423	0
6		Infiltration Galleries and Tunnels	-	-	-
7		Supply Mains	-	-	-
8		Power Generation Equipment	-	-	-
9		Electrical Pumping Equipment	341,101	341,101	0
10		Water Treatment Equipment	2,167	0	(2,167)
11		Water Treatment Plant	-	-	-
12		Chemical Solution Feeders	-	2,167	2,167
13		Distribution Reservoirs & Standpipe	64,318	-	(64,318)
14		Storage Tanks	-	27,712	27,712
15		Pressure Tanks	-	32,553	32,553
16		Transmission and Distribution Mains	139,059	135,201	(3,858)
17		Services	40,947	40,947	-
18		Meters	17,066	17,066	-
19		Hydrants	12,984	12,984	-
20		Backflow Prevention Devices	-	-	-
21		Other Plant & Miscellaneous Equipment	35,847	35,847	-
22		Office Furniture & Fixtures	-	-	-
23		Computers & Software	-	-	-
24		Transportation Equipment	-	-	-
25		Stores Equipment	-	-	-
26		Tools and Work Equipment	-	-	-
27		Laboratory Equipment	-	-	-
28		Power Operated Equipment	-	-	-
29		Communications Equipment	-	-	-
30		Miscellaneous Equipment	-	-	-
31		Other Tangible Plant	-	-	-
			$ 731,197	$ 723,287	$ (7,910)

References:
Col [A]: Company Schedule B-1
Col [B]: GLF Testimony, RUCO DR 2.12
Col [C]: Col. [A] + Col. [B]

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Surrebuttal Schedule GLF-10.1

ORIGINAL COST RATE BASE ADJUSTMENT # 7 - REDUCE AIAC

LINE NO.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1	108	Accumulated Depreciation	2,101,905	$ (128,600)	$ 1,973,305

References:
Col [A]: Company Schedule B-1
Col [B]: GLF Testimony
Col [C]: Col. [A] + Col. [B]

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Surrebuttal Schedule GLF-10.2

ORIGINAL COST RATE BASE ADJUSTMENT # 8 - ACCUMULATED DEFERRED INCOME TAX

LINE NO.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1		Accumulated Deferred Income Tax	135,342	$ (16,836)	$ 118,506

References:
Col [A]: Company Schedule B-1
Col [B]: GLF Testimony
Col [C]: Col. [A] + Col. [B]

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OPERATING INCOME STATEMENT - ADJUSTED TEST YEAR AND STAFF RECOMMENDED

LINE NO.	DESCRIPTION	[A] COMPANY ADJUSTED TEST YEAR AS FILED	[B] STAFF TEST YEAR ADJUSTMENTS	[C] STAFF TEST YEAR AS ADJUSTED	[D] STAFF PROPOSED CHANGES	[E] STAFF RECOMMENDED
1	*OPERATING REVENUES:*					
2	Metered Water Revenues	$ 559,013	$ 21,708	$ 580,721	$ 180,824	$ 761,545
3	Unmetered Water Revenues	-	-	-	-	-
4	Other Water Revenues	13,738	-	13,738		13,738
5	**Total Operating Revenues**	$ 572,751	$ 21,708	$ 594,459	$ 180,824	$ 775,283
6						
7	*OPERATING EXPENSES:*					
8	Salaries and Wages	$ 40,000	$ -	$ 40,000	$ -	$ 40,000
9	Employee Pensions & Benefits	-	-	-	-	-
10	Purchased Water	-	-	-	-	-
11	Purchased Power	27,066	577	27,643	-	27,643
12	Chemicals	-	-	-	-	-
13	Repairs and Maintenance	7,746	-	7,746	-	7,746
14	Office Supplies and Expense	14,855	-	14,855	-	14,855
15	Outside Services	102,925	-	102,925	-	102,925
16	Water Testing	1,215	1,568	2,783	-	2,783
17	Rents	-	-	-	-	-
18	Transportation Expenses	-	-	-	-	-
19	Insurance - General Liability	9,669	-	9,669	-	9,669
20	Insurance - Health and Life	-	-	-	-	-
21	Advertising	-	-	-	-	-
22	Regulatory Comm Expense - Rate Case	20,000	20,000	40,000	-	40,000
23	Regulatory Comm Expense - Other	378	-	378	-	378
24	Bad Debt Expense	-	-	-	-	-
25	Miscellaneous Expense	-	-	-	-	-
26	Depreciation and Amortization	227,855	11,047	238,902	-	238,902
27	Interest on Security Deposits	-	-	-	-	-
28	Taxes other than Income	2,988	-	2,988	-	2,988
29	Property Taxes	21,299	(2,250)	19,049	1,798	20,846
30	Income Tax	22,873	(10,969)	11,904	72,964	84,867
31	**Total Operating Expenses**	$ 498,869	$ 19,973	$ 518,842	$ 74,761	$ 593,603
32						
33	**Operating Income**	$ 73,882	$ 1,735	$ 75,617	$ 106,063	$ 181,680

References:
Column [A]: Company Schedule C-1
Column [B]: Schedule GLF-12
Column [C]: Column [A] + Column [B]
Column [D]: Schedules GLF-1 and GLF-2
Column [E]: Column [C] + Column [D]

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Surrebuttal Schedule GLF-12

SUMMARY OF OPERATING INCOME STATEMENT ADJUSTMENTS - TEST YEAR

LINE NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] GLF-13 Revenue Annualization ADJ #1	[C] GLF-14 Rate Case Exp ADJ #2	[D] GLF-15 Water Testing ADJ # 3	[E] GLF-16 Depreciation Exp ADJ #4	[F] GLF-17 Property Taxes ADJ #5	[G] GLF-18 Income Taxes ADJ #6	[H] GLF-18.1 An Pur Pwr ADJ #7	[I] STAFF ADJUSTED
1	*Operating Revenues:*									
2	Metered Water Revenues	$ 559,013	$ 21,708		$ -	$ -	$ -	$ -	$ -	$ 580,721
3	Unmetered Water Revenues	-	-		-	-	-	-	-	-
4	Other Water Revenues	13,738	-		-	-	-	-	-	13,738
5	Total Operating Revenues	$ 572,751	$ 21,708	$ -	$ -	$ -	$ -	$ -	$ -	$ 594,459
6										
7	*Operating Expenses:*									
8	Salaries and Wages	$ 40,000	$ -	$ -	$ -	$ -	$ -	$ -	$ -	40,000
9	Employee Pensions & Benefits	-	-	-	-	-	-	-	-	-
10	Purchased Water	-	-	-	-	-	-	-	-	-
11	Purchased Power	27,066	-	-	-	-	-	-	577	27,643
12	Chemicals	-	-	-	-	-	-	-	-	-
13	Repairs and Maintenance	7,746	-	-	-	-	-	-	-	7,746
14	Office Supplies and Expense	14,855	-	-	-	-	-	-	-	14,855
15	Outside Services	102,925	-	-	-	-	-	-	-	102,925
16	Water Testing	1,215	-	-	1,568	-	-	-	-	2,783
17	Rents	-	-	-	-	-	-	-	-	-
18	Transportation Expenses	-	-	-	-	-	-	-	-	-
19	Insurance - General Liability	9,669	-	-	-	-	-	-	-	9,669
20	Insurance - Health and Life	-	-	-	-	-	-	-	-	-
21	Advertising	-	-	-	-	-	-	-	-	-
22	Regulatory Comm Expense - Rate Case	20,000	-	20,000	-	-	-	-	-	40,000
23	Regulatory Comm Expense - Other	378	-	-	-	-	-	-	-	378
24	Bad Debt Expense	-	-	-	-	-	-	-	-	-
25	Miscellaneous Expense	-	-	-	-	-	-	-	-	-
26	Depreciation and Amortization	227,855	-	-	-	11,047	-	-	-	238,902
27	Interest on Security Deposits	-	-	-	-	-	-	-	-	-
28	Taxes other than Income	2,988	-	-	-	-	-	-	-	2,988
29	Property Taxes	21,299	-	-	-	-	(2,250)	-	-	19,049
30	Income Tax	22,873	-	-	-	-	-	(10,969)	-	11,904
31	Total Operating Expenses	$ 498,869	$ -	$ 20,000	$ 1,568	$ 11,047	$ (2,250)	$ (10,969)	$ 577	$ 518,842
	Operating Income	$ 73,882	$ 21,708	$ (20,000)	$ (1,568)	$ (11,047)	$ 2,250	$ 10,969	$ (577)	$ 75,617

References:
Column [A]: Company Schedule C-1
Column [B] - [G] : Schedule GTM-13 through GTM-17
Column [C]: Add Column [A] - Column [F]

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Surrebuttal Schedule GLF-13

OPERATING INCOME ADJUSTMENT # 1 - REVENUE ANNUALIZATION

LINE NO.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1		Metered Water Revenues	$ 559,013	$ 21,708	$ 580,721

References:
Col [A]: Company Schedeule B-1
Col [B]: GLF Testimony
Col [C]: Col. [A] + Col. [B]

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Surrebuttal Schedule GLF-14

OPERATING INCOME ADJUSTMENT # 2 - RATE CASE EXPENSE

LINE NO.	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1	Regulatory Commission Expense - Rate Case	$ 20,000	$ 20,000	$ 40,000

References:
Column [A]: Company Schedule C-1
Column [B]: GLF Testimony
Col [C]: Col. [A] + Col. [B]

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Surrebuttal Schedule GLF-15

OPERATING INCOME ADJUSTMENT # 3 - WATER TESTING EXPENSE

LINE NO.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1		Water Testing	$ 1,215	$ 1,568	$ 2,783

References:
Col [A]: Company Schedule B-1
Col [B]: GLF Testimony
Col [C]: Col. [A] + Col. [B]

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OPERATING INCOME ADJUSTMENT # 4 - DEPRECIATION EXPENSE

LINE NO.	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1	Depreciation and Amortization	$ 227,855	$ 11,047	$ 238,902

Line No.	ACCT NO.	DESCRIPTION	[A] Company Proposed PLANT IN SERVICE BALANCE	[B] STAFF DEPR. PLANT BALANCE	[C] STAFF RECOMMENDED RATE	[D] STAFF RECOMMENDED EXPENSE
		Plant In Service				
2	301	Organization Cost	$ 127,103	127,103	0.00%	$ -
3	302	Franchise Cost	-	-	0.00%	-
4	303	Land and Land Rights	494,159	114,322	0.00%	-
5	304	Structures and Improvements	182,570	182,570	3.33%	6,080
6	305	Collecting and Impounding Res.	-	-	2.50%	-
7	306	Lake River and other Intakes	-	-	2.50%	-
8	307	Wells and Springs	386,591	386,591	3.33%	12,873
9	308	Infiltration Galleries and Tunnels	-	-	6.67%	-
10	309	Supply Mains	-	-	2.00%	-
11	310	Power Generation Equipment	-	-	5.00%	-
12	311	Electrical Pumping Equipment	968,652	968,652	12.50%	121,082
13	320.0	Water Treatment Equipment	15,947	-		-
14	320.1	Water Treatment Plant	-	-	3.33%	-
15	320.2	Chemical Solution Feeders	-	15,947	20.00%	3,189
16	330	Distribution Reservoirs & Standpipe	836,890	-		-
17	330	Storage Tanks	-	312,477	2.22%	6,937
18	330	Pressure Tanks	-	452,063	5.00%	22,603
19	331	Transmission and Distribution Mains	1,611,320	1,482,720	2.00%	29,654
20	333	Services	386,947	386,947	3.33%	12,885
21	334	Meters	94,263	94,263	8.33%	7,852
22	335	Hydrants	161,737	161,737	2.00%	3,235
23	336	Backflow Prevention Devices	-	-	6.67%	-
24	339	Other Plant & Miscellaneous Equipment	187,582	187,582	6.67%	12,512
25	340	Office Furniture & Fixtures	-	-	6.67%	-
26	340	Computers & Software	-	-	20.00%	-
27	341	Transportation Equipment	-	-	20.00%	-
28	342	Stores Equipment	-	-	4.00%	-
29	343	Tools and Work Equipment	-	-	5.00%	-
30	344	Laboratory Equipment	-	-	10.00%	-
31	345	Power Operated Equipment	-	-	5.00%	-
32	346	Communications Equipment	-	-	10.00%	-
33	347	Miscellaneous Equipment	-	-	10.00%	-
34	348	Other Tangible Plant	-	-	3.33%	-
35	-	Rounding Amount	-	-	67.00%	
36		Subtotal General	$ 5,453,761	$ 4,872,974		$ 238,902
37		Less: Non- depreciable Account(s)	621,262	241,425		
38		Depreciable Plant (L29-L30)	$ 4,832,499	$ 4,631,549		
39		Contributions-in-Aid-of-Construction (CIAC)			$ -	
40		Weighted Average Depreciation/Amortization Rate			5.1582%	
41		Less: Amortization of CIAC (L32 x L33)				$ -
42		**Depreciation Expense - STAFF [Col. (C), L36 - L41]**				$ 238,902

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Surrebuttal Schedule GLF-17

OPERATING INCOME ADJUSTMENT # 5 - PROPERTY TAXES

LINE NO.	Property Tax Calculation	[A] STAFF AS ADJUSTED	[B] STAFF RECOMMENDED
1	Staff Adjusted Test Year Revenues - 2009	$ 594,459	$ 594,459
2	Weight Factor	2	2
3	Subtotal (Line 1 * Line 2)	$ 1,188,918	$ 1,188,918
4a	Staff Adjusted Test Year Revenues - 2006	594,459	
4b	Staff Recommended Revenue, Per Schedule GLF-1		775,283
5	Subtotal (Line 4 + Line 5)	$ 1,783,377	$ 1,964,201
6	Number of Years	3	3
7	Three Year Average (Line 5 / Line 6)	$ 594,459	$ 654,734
8	Department of Revenue Mutilplier	2	2
9	Revenue Base Value (Line 7 * Line 8)	$ 1,188,918	$ 1,309,467
10	Plus: 10% of CWIP -		-
11	Less: Net Book Value of Licensed Vehicles		-
12	Full Cash Value (Line 9 + Line 10 - Line 11)	$ 1,188,918	$ 1,309,467
13	Assessment Ratio	20.0%	20.0%
14	Assessment Value (Line 12 * Line 13)	237,784	$ 261,893
15	Composite Property Tax Rate (Per Company Schedule C-2, Page 3, Line 16)	7.4558%	7.4558%
16	Property Tax Expense - Excludes Parcels (Line 14 * Line 15)	$ 17,729	$ 19,526
17	Tax of Parcels	$ 1,320	$ 1,320
18	Staff Recommended Test Year Property Tax (Line 16 + Line 17)	$ 19,049	
19	Company Proposed Property Tax	21,299	
20	Staff Test Year Adjustment (Line 18-Line 19)	$ (2,250)	
21	Property Tax - Staff Recommended Revenue (Line 16 + Line 17)		$ 20,846
22	Staff Test Year Adjusted Property Tax Expense (Line 18)		$ 19,049
23	Increase/(Decrease) to Property Tax Expense Line 21 - Line 22)		$ 1,798
24	Increase to Property Tax Expense		$ 1,798
25	Increase in Revenue Requirement		180,824
26	Increase to Property Tax per Dollar Increase in Revenue (Line24/Line 25)		0.994107%

References:
Col [A]: Company Schedule C-1 Page 3
Col [B]: GLF Testimony

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Surrebuttal Schedule GLF-18

OPERATING INCOME ADJUSTMENT # 6 - INCOME TAXES

LINE NO.	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1	Income Tax	$ 22,873	$ (10,969)	$ 11,904
2				
3				
4				
5				
6				
7				
8				
9				
10				
11	References:			
12	Col [A]: Company Schedule C-1 Page 3			
13	Col [B]: Column [C] - Column [A]			
14	Col [C]: Schedule GLF-2			

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Surrebuttal Schedule GLF-18.1

OPERATING INCOME ADJUSTMENT # 7 - ANNUALIZE PURCHASED POWER

LINE NO.	Account Number	DESCRIPTION	[A] COMPANY PROPOSED	[B] STAFF ADJUSTMENTS	[C] STAFF RECOMMENDED
1		Purchased Power	$ 27,066	$ 577	$ 27,643

References:
Col [A]: Company Schedeule B-1
Col [B]: GLF Testimony
Col [C]: Col. [A] + Col. [B]

RATE DESIGN

Monthly Usage Charge (all classes	Present Rates	Company Proposed Rates	Staff Recommended Rates
5/8" Meter - All Classes	$ 42.20	$ 56.97	$ 51.00
3/4" Meter - All Classes	$ 63.30	$ 85.46	$ 76.50
1" Meter - All Classes	$ 105.50	$ 142.43	$ 128.00
1½" Meter - All Classes	$ 211.50	$ 284.85	$ 255.00
2" Meter - All Classes	$ 339.68	$ 455.76	$ 408.00
3" Meter - All Classes	$ 675.20	$ 911.52	$ 816.00
4" Meter - All Classes	$ 1,055.00	$ 1,424.25	$ 1,275.00
6" Meter - All Classes	$ 2,110.00	$ 2,848.50	$ 2,550.00
Construction/Stand pipe	N/A	N/A	N/A
Commodity Rates (all classes)			
5/8" Meter			
From 1 to 3,000 Gallons	$ 3.95	$ 6.80	$ 4.80
From 3,001 to 9,000 Gallons	$ 5.91	$ 10.92	$ 9.75
Over 9,000 Gallons	$ 7.11	$ 13.13	$ 11.75
3/4" Meter			
From 1 to 3,000 Gallons	$ 3.95	$ 6.80	$ 4.80
From 3,001 to 9,000 Gallons	$ 5.91	$ 10.92	$ 9.75
Over 10,000 Gallons	$ 7.11	$ 13.13	$ 11.75
1" Meter			
From 1 to 22,500 Gallons	$ 5.91	$ 10.92	$ 9.75
Over 22,500 Gallons	$ 7.11	$ 13.13	$ 11.75
1½" Meter			
From 1 to 34,000 Gallons	$ 5.91	$ 10.92	$ 9.75
Over 34,000 Gallons	$ 7.11	$ 13.13	$ 11.75
2" Meter			
From 1 to 45,000 Gallons	$ 5.91	$ 10.92	$ 9.75
Over 45,000 Gallons	$ 7.11	$ 13.13	$ 11.75
3" Meter			
From 1 to 68,000 Gallons	$ 5.91	$ 10.92	$ 9.75
Over 68,000 Gallons	$ 7.11	$ 13.13	$ 11.75
4" Meter			
From 1 to 90,000 Gallons	$ 5.91	$ 10.92	$ 9.75
Over 90,000 Gallons	$ 7.11	$ 13.13	$ 11.75
6" Meter (Res., Comm.)			
From 1 to 135,000 Gallons	$ 5.91	$ 10.92	$ 9.75
Over 135,000 Gallons	$ 7.11	$ 13.13	$ 11.75
Construction/Stand pipe (Res., Comm.)			
All Gallons	$ 7.11	$ 13.13	$ 11.75

	Present	Co. Proposed			Staff Recommended		
Service Line and Meter Installation Charges	Total	Line	Meter	Total	Line	Meter	Total
5/8" Meter	$ 225	$ 385	$ 135	$ 520	$ 385	$ 135	$ 520
3/4" Meter	270	415	205	620	415	205	620
1" Meter	300	465	265	730	465	265	730
1½" Meter	425	520	475	995	520	475	995
2" Turbine Meter	550	800	995	1,795	800	995	1,795
2" Compound Meter	550	800	1,840	2,640	800	1,840	2,640
3" Turbine Meter	750	1,015	1,620	2,635	1,015	1,620	2,635
3" Compound Meter	750	1,135	2,495	3,630	1,135	2,495	3,630
4" Turbine Meter	1,375	1,430	2,570	4,000	1,430	2,570	4,000
4" Compound Meter	1,375	1,610	3,545	5,155	1,610	3,545	5,155
6" Turbine Meter	2,800	2,150	4,925	7,075	2,150	4,925	7,075
6" Compound Meter	2,800	2,270	6,820	9,090	2,270	6,820	9,090
8"	Cost	Cost	Cost	Cost	Cost	Cost	Cost
10"	Cost	Cost	Cost	Cost	Cost	Cost	Cost
12"	Cost	Cost	Cost	Cost	Cost	Cost	Cost

Service Charges	Present	Co. Proposed	Staff Recommended
Establishment	$ 50.00	$ 50.00	$ 50.00
Establishment (After Hours)	75.00	75.00	NT
Reconnection (delinquent)	75.00	75.00	75.00
Reconnection (after hours)	50.00	50.00	NT
Meter Test	20.00	20.00	20.00
Deposit Requirement (Residential)	(a)	(a)	(a)
Deposit Requirement (None Residential Meter)	(a)	(a)	(a)
Deposit Interest	6.00%	6.00%	6.00%
Re-Establishment (With-in 12 Months)	(b)	(b)	(b)
NSF Check	15.00	15.00	15.00
Deferred Payment, Per Month	1.5%	1.50%	1.50%
Meter Re-Read	20.00	20.00	20.00
Late Charge per month	1.5%	1.5%	1.5%
Customer Requested Meter Test	20.00	20.00	20.00
After Hours Service Charge	10.00	10.00	50.00
Turn-on/off (at customer request)	NT	75.00	NT
Moving Customer Meter (at customer request)	NT	cost	cost

NT = No Tariff

Monthly Service Charge for Fire Sprinkler	Present	Co. Proposed	Staff Recommended
All Meter Sizes			Greater of $10 or 2 percent of the general service rate for a similar size meter.

Per Commission Rules (R14-2-403.B)
(a) Residential - two times the average bill. Non-residential - two and one-half times the average bill.
(b) Minimum charge times number of months disconnected.

In addition to the collection of regular rates, the utility will collect from its customers a proportionate share of any privelege, sales, use, and franchise tax. Per Commission Rule (14-2-409.D.5).
All advances and/or contributions are to include labor, materials, overheads and all applicable taxes,
Cost to include labor, materials and parts, overheads and all applicable taxes.

Typical Bill Analysis
Residential 5/8 Inch Meter

Company Proposed	Gallons	Present Rates	Proposed Rates	Dollar Increase	Percent Increase
Average Usage	5,477	$ 66.73	$ 100.30	$ 33.57	50.31%
Median Usage	4,500	60.96	89.63	$ 28.68	47.04%
Staff Recommended					
Average Usage	5,477	$ 66.73	$ 89.55	$ 22.82	34.20%
Median Usage	4,500	60.96	80.03	$ 19.07	31.29%

Present & Proposed Rates (Without Taxes)
Residential 5/8 Inch Meter

Consumption	Rates	Rates	Increase	Rates	Increase
-	$ 42.20	$ 56.97	35.00%	$ 51.00	20.85%
1,000	46.15	63.77	38.18%	55.80	20.91%
2,000	50.10	70.57	40.86%	60.60	20.96%
3,000	54.05	77.37	43.15%	65.40	21.00%
4,000	58.00	84.17	45.12%	75.15	29.57%
4,500	60.96	89.63	47.04%	80.03	31.29%
5,000	63.91	95.09	48.79%	84.90	32.84%
5,477	66.73	100.30	50.31%	89.55	34.20%
6,000	69.82	106.01	51.83%	94.65	35.56%
7,000	75.73	116.93	54.40%	104.40	37.86%
8,000	81.64	127.85	56.60%	114.15	39.82%
9,000	87.55	138.77	58.50%	123.90	41.52%
10,000	94.66	151.90	60.47%	135.65	43.30%
11,000	101.77	165.03	62.16%	147.40	44.84%
12,000	108.88	178.16	63.63%	159.15	46.17%
13,000	115.99	191.29	64.92%	170.90	47.34%
14,000	123.10	204.42	66.06%	182.65	48.38%
15,000	130.21	217.55	67.08%	194.40	49.30%
16,000	137.32	230.68	67.99%	206.15	50.12%
17,000	144.43	243.81	68.81%	217.90	50.87%
18,000	151.54	256.94	69.55%	229.65	51.54%
19,000	158.65	270.07	70.23%	241.40	52.16%
20,000	165.76	283.20	70.85%	253.15	52.72%
25,000	201.31	348.85	73.29%	311.90	54.94%
30,000	236.86	414.50	75.00%	370.65	56.48%
35,000	272.41	480.15	76.26%	429.40	57.63%
40,000	307.96	545.80	77.23%	488.15	58.51%
45,000	343.51	611.45	78.00%	546.90	59.21%
50,000	379.06	677.10	78.63%	605.65	59.78%
75,000	556.81	1,005.35	80.56%	899.40	61.53%
100,000	734.56	1,333.60	81.55%	1,193.15	62.43%

BEFORE THE ARIZONA CORPORATION COMMISSION

GARY PIERCE
Chairman
BOB STUMP
Commissioner
SANDRA D. KENNEDY
Commissioner
PAUL NEWMAN
Commissioner
BRENDA BURNS
Commissioner

IN THE MATTER OF THE APPLICATION OF GOODMAN WATER COMPANY, AN ARIZONA CORPORATION, FOR (i) A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND (ii) AN INCREASE IN ITS WATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.	DOCKET NO. W-02500A-10-0382

SURREBUTTAL

TESTIMONY

OF

MARLIN SCOTT, JR.

UTILITIES ENGINEER

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

JUNE 13, 2011

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SURREBUTTAL SUMMARY
GOODMAN WATER COMPANY
DOCKET NO. W-02500-10-0382

CONCLUSION/RECOMMENDATIONS

A. Staff believes its growth projection should be used because the data used is the actual data obtained from Goodman Water Company ("Company") and this data shows a growth pattern appropriate for this economic climate.

B. Staff revised its plant-in-service adjustment totaling to $128,600 for plant items considered not used and useful in this proceeding.

C. Staff accepts of the Company's position that the Water Plant No. 3's storage tank is actually a 600,000 gallon tank with a useable capacity of 487,000 gallons. In addition, the Company states that the 190,000 gallon "upsizing" of the Water Plant No. 3 storage tank at a cost of $72,350 was not part of this rate case. Based on these factors, Staff is willing to withdraw any adjustment and considers the 340,000 gallon storage tank, which is really a 410,000 gallon tank, used and useful for purposes of this rate proceeding.

D. Staff recommends that the Company file with Docket Control, as a compliance item in this docket and within 90 days of the effective date of a decision in this proceeding, at least five Best Management Practices ("BMPs") in the form of tariffs that substantially conform to the templates created by Staff for Commission's review and consideration. These BMP templates are available on the Commission's website. A maximum of two BMPs may come from the "Public Awareness/Public Relations" or "Education and Training" categories. The Company may request cost recovery of the actual costs associated with the BMPs implemented in its next general rate application.

INTRODUCTION

Q. Please state your name, place of employment and job title.

A. My name is Marlin Scott, Jr. My place of employment is the Arizona Corporation Commission ("Commission"), Utilities Division, 1200 West Washington Street, Phoenix, Arizona 85007. My job title is Utilities Engineer.

Q. Are you the same Marlin Scott, Jr. who submitted Direct Testimony on behalf of the Utilities Division?

A. Yes.

Q. What was the purpose of that testimony?

A. My Direct Testimony provided the Utilities Division Staff's ("Staff") engineering evaluation of Goodman Water Company ("Company") for this proceeding.

Q. What is the purpose of your Surrebuttal Testimony?

A. To provide Staff's response to the Company's Rebuttal Testimony on three issues; 1) growth projection, 2) plant not used and useful, and 3) excess storage tank capacity. Staff's response to the excess storage tank capacity issue will also be in response to the intervener's rebuttal testimony. Staff will also provide a recommendation for the Company to submit Best Management Practice Tariffs.

GROWTH PROJECTION

Q. Have you reviewed the rebuttal testimony of Mark F. Taylor regarding growth projection?

A. Yes.

Q. What was Mr. Taylor's conclusion regarding the growth projection?

A. Mr. Taylor did not agree with Staff's estimated growth projection of 875 customers by 2014 using the 2009 test year customer base of 621 and the 5-year customer growth projection based on historical growth after the test year. In fact, Mr. Taylor suggested that this rate case proceeding not use the 2009 test year data but use data ending in 2007 or 2008 which would project customer growth of 1,113 and 1,112 by 2012 and 2013, respectively.

Q. Does Staff agree with Mr. Taylor's conclusion?

A. No.

Q. Why not?

A. First, this Commission uses test year data in determining rates. The Company selected the test year ending December 31, 2009 and therefore, data from the test year should be used. Second, if Mr. Taylor's suggested growth projection was used in this rate proceeding, then his projected customer base of 820 and 725 as shown for 2009 in both graphs of his Rebuttal's Appendix E is much higher than the actual 2009 test year customer base of 621.

Q. Does Staff still recommend the use of its growth projection?

A. Yes. Staff believes its growth projection should be used because the data used is the actual data obtained from the Company and this data shows a growth pattern appropriate for this economic climate.

PLANT NOT USED AND USEFUL

Q. Have you reviewed the rebuttal testimony of Mr. Taylor regarding plant items not used and useful?

A. Yes.

Q. What was Mr. Taylor's conclusion regarding these plant items?

A. Mr. Taylor did not disagree or agree with Staff's plant adjustments that were considered not used and useful. Mr. Taylor only provided reasons why certain water mains were installed, but did not dispute Staff's position that these certain water mains were not in service nor providing service to customers.

Q. What is Staff's response?

A. As a summary, Staff's list of plant items considered not used and useful in its Direct Testimony is as follows:

Acct. No.	Plant Facilities	Year Installed	Original Cost
331	Transmission & Distribution Mains		
	1. From Water Plant #1 to Proposed Well Site #3:		
	a. 12-inch main w/ appurtenances at 974 feet.	2008	$50,586
	b. 12-inch main w/ appurtenances at 524 feet. ($28,470 not yet recorded)		N/A
	c. 12-inch main w/ appurtenances at 1,571 feet. ($94,197 not yet recorded)		N/A
	2. From Edwin Road to end of line (southwest corner): 12-inch main w/ appurtenances at 310 feet.	2002	$14,600
	3. Phase 5 - Main on Running Roses Lane: 8-inch main w/ appurtenances at 764 feet	2008	$40,378
	Direct Testimony Total:		**$105,564**

In addition to the above three identified water mains, Staff also noted in its Direct Testimony that Staff was awaiting a response to a data request and that any further plant-in-service adjustment and recommendation related to its Tenth Set of Data Requests would be provided in its Surrebuttal. Below is Staff's plant adjustment of $23,036 related to the Company's response to Staff's Tenth Data Request.

Acct. No.	Plant Facilities	Year Installed	Original Cost
331	Transmission & Distribution Mains 4. Phase 4 - Main on Sparkle Spur Lane: 8-inch main w/ appurtenances at 308 feet and 6-inch main w/ appurtenances at 140 feet	2007	$23,036
	Surrebuttal Testimony Total:		**$23,036**
	Direct Testimony Total:		**$105,564**
	TOTAL:		**$128,600**

As a final result, Staff's total adjustment for plant items not used and useful is $128,600 as shown above. It is still Staff's position that the above identified water mains are considered not used and useful because these mains do not provide service to customers.

EXCESS STORAGE TANK CAPACITY

Q. First, could you provide a definition of excess capacity and brief description on how Staff determines if any plant facility has excess capacity?

A. Yes. Staff defines excess capacity to mean constructed plant facilities that exceed the system requirements within a reasonable planning period. Staff typically uses peak demand factors as the requirement and 5 years as a reasonable planning period. Any operating plant facility needed beyond the 5-year planning period may be considered excess capacity. In other words, excess capacity exists when the installed plant capacity exceeds what is needed to accommodate reasonable growth. The 5-year growth projection enables utilities to provide new service connections for a reasonable period. This approach is also consistent with how Staff handles this issue in other applications it analyzes.

Q. Have you reviewed the rebuttal testimony of Mr. Taylor regarding excess storage tank capacity?

A. Yes.

Q. What was Mr. Taylor's conclusion regarding the excess storage tank capacity?

A. Mr. Taylor did not agree with Staff's position that the Company's 530,000 gallon storage tank had excess capacity. Mr. Taylor based his conclusion by using; 1) design requirements for demand assumption of 2.8 persons per household at 100 gallons person per day, or average daily demand of 280 gallons per day per service connection, 2) identifying "dead storage" versus "usable" volume of storage capacity, and 3) using his growth projection.

Q. Does Staff agree with Mr. Taylor's conclusion?

A. No.

Q. Why not?

A. First, Staff would like to point out that the 530,000 gallon storage tank is actually a 600,000 gallon storage tank. The data that determined the size of this tank to be 600,000 gallons came from Mr. Taylor's Rebuttal – Appendix B where the Water Plant No. 3 schematic showed the tank dimension of 72 feet in diameter by 20 feet in height.

For the test year ending December 2009, the Company submitted a Water Use Data Sheet ("WUDS") to show the demand placed on its water system. The WUDS shows the actual peak month demand placed on the water system by the test year customer base. Staff always uses the actual use data when it is available to determine an appropriate capacity and not the "design" demand consumption factors used by Mr. Taylor.

Since the storage tank is actually a 600,000 gallon tank, Staff re-evaluated its storage capacity calculation. Staff also took into consideration the Company's 487,000 gallons of useable capacity in its re-evaluation. Staff also accepted the Company's position that the 190,000 gallon "upsizing" of the Water Plant No. 3 storage tank at a cost of $72,350 was not part of this rate case. Based on the above factors, Staff is willing to withdraw any adjustment and considers the 340,000 gallon storage tank, which is really a 410,000 gallon tank, used and useful for purposes of this rate proceeding. Staff revised calculations are shown in EXHIBIT MSJ-1 to this testimony.

Q. Have you reviewed the rebuttal testimony of the intervener, Lawrence Wawrzyniak regarding excess storage tank capacity?

A. Yes.

Q. What was Mr. Wawrzyniak's concern regarding the excess storage tank capacity?

A. Mr. Wawrzyniak did not agree with Staff's use of a commercial fire flow requirement and how this effected the storage capacity requirement.

Q. What is Staff's response?

A. It is Staff's understanding that there are different fire flow requirements for this water system; 2,000 GPM at 2 hours for commercial and 1,000 to 1,500 GPM at 2 hours for residential. In its initial evaluation process, Staff took the highest fire flow requirement, which is the commercial requirement, as the governing fire flow to calculate the required storage capacity. Although there are commercial lots available but no commercial customers at this time, Staff used the commercial fire flow requirement because the Company's service area identified the commercial zoning area, sized plant facilities to accommodate the commercial zoning area, and water service is readily available upon request. Therefore, Staff believes it is reasonable to use the commercial fire flow requirement.

After Staff conducted its initial evaluation of the required storage capacity, Staff further evaluated the storage tank at Water Plant No. 3 and its operation. The operation of this storage tank indicated that this tank was needed to provide the fire flow requirement to K-Zone residential customers located in the northern-most upper zone area of the water system. Therefore, Staff included the fire flow requirement of 1,500 GPM at 2 hours in the evaluation of Water Plant No. 3's storage tank. As part of this Surrebuttal, Staff re-evaluated the storage tank capacity calculation as shown in EXHIBIT MSJ-1 to this testimony.

BEST MANAGEMENT PRACTICES TARIFFS

Q. Could you provide a brief background of the Best Management Practices.

A. Yes. In 2008, the Arizona Department of Water Resources ("ADWR") added a new regulatory program for the ADWR Third Management Plan for Active Management Areas ("AMAs"). The new program, called Modified Non-Per Capita Conservation Program

("Modified NPCCP"), addresses large municipal water providers (cities, towns and private water companies serving more than 250 acre-feet per year) and was developed in conjunction with stakeholders from all AMAs. Participation in the program is required for all large municipal water providers in AMA's that do not have a Designation of Assured Water Supply and that are not regulated as a large untreated water provider or an institutional provider.

The Modified NPCCP is a performance-based program that requires participating providers to implement water conservation measures that result in water use efficiency in their service areas. A water provider regulated under the program must implement a required Public Education Program and choose one or more additional Best Management Practices ("BMPs") based on its size, as defined by its total number of water service connections. The provider must select the additional BMPs from the list included in the Modified NPCCP Program. The BMPs are a mix of technical, policy, and information conservation efforts.

Although the implementation of the Modified NPCCP is required of large municipal water providers within an AMA, the Commission has previously adopted the BMPs for implementation by Commission regulated water companies.

Q. In its Direct Testimony, did Staff provide a recommendation regarding BMPs?

A. No. However, Staff believes that the filing of this Surrebuttal provides the opportunity for Staff to present a discussion and recommendation for the BMPs for Commission consideration.

Q. What is Staff's recommendation regarding the BMPs?

A. Staff recommends that the Company file with Docket Control, as a compliance item in this docket and within 90 days of the effective date of a decision in this proceeding, at least five BMPs in the form of tariffs that substantially conform to the templates created by Staff for Commission's review and consideration. These BMP templates are available on the Commission's website. A maximum of two BMPs may come from the "Public Awareness/Public Relations" or "Education and Training" categories. The Company may request cost recovery of the actual costs associated with the BMPs implemented in its next general rate application.

Q. Does this conclude your Surrebuttal Testimony?

A. Yes.

RE-EVALUATION OF EXCESS STORAGE TANK CAPACITY

The storage tank capacity totaling 1,000,000 gallons (= 400,000 + 600,000), minus the fire flow requirement (2,000 GPM at 2 hours = 240,000 GPD), could adequately serve up to approximately 3,300 connections (= (1,000,000 - 240,000) / 230). For this proceeding, the 600,000 gallon tank is divided into 410,000 gallon and 190,000 gallon (upsized) capacities.

The usable storage tank capacity totaling 803,000 gallons (= 316,000 + 487,000), minus the fire flow requirement (2,000 GPM at 2 hours = 240,000 GPD), could adequately serve up to approximately 2,450 connections (= (803,000 - 240,000) / 230).

As shown above, the total storage tank capacity of 1,000,000 gallons, **with 803,000 gallons of usable capacity**, could have excess capacity. To further evaluate how much of the **usable** storage tank capacity is excessive, Staff considered the following:

1. Within a 5-year period, Staff estimated the required storage capacity to be 441,250 GPD. This amount is calculated by the fire flow requirement (240,000 GPD) plus the demand in five years at 201,250 GPD (= 230 GPD/connection x 875 connections), totaling to 441,250 GPD.

2. The entire 400,000 gallon storage tank, **with 316,000 gallons of useable capacity**, is needed because both wells pump into this tank and this tank serves as the chlorination contact time chamber. In addition, this tank serves as the main storage for fire flow protection for the majority of the water system.

3. Staff estimated the 5-year projected storage capacity at 441,250 GPD which is more than the **316,000 gallons of usable capacity by 125,250 gallons.**

4. To determine how much of the 600,000 gallon storage tank, **with 487,000 gallons of useable capacity**, is needed, Staff considered the fire flow of 180,000 gallons (=1,500 GPM at 2 hours) for the K-Zone customers plus the 125,250 gallons **totaling to 305,250 gallons of required capacity.**

5. **The 305,250 gallons of required capacity is 63% of the 487,000 gallons of useable capacity**. However, the Company has claimed that the upsized 190,000 gallon of tank capacity is not part of the rate case, which would reduce the useable tank capacity to 297,000 gallons (= 487,000 – 190,000). Since the 305,250 gallons of required capacity is more than the 297,000 gallons of useable capacity by 8,250 gallons, Staff concludes that the Water Plant No. 3's storage tank capacity of 410,000 gallons is not excessive for this rate proceeding.

BEFORE THE ARIZONA CORPORATION COMMISSION

GARY PIERCE
Chairman
BOB STUMP
Commissioner
SANDRA D. KENNEDY
Commissioner
PAUL NEWMAN
Commissioner
BRENDA BURNS
Commissioner

IN THE MATTER OF THE APPLICATION OF GOODMAN WATER COMPANY, AN ARIZONA CORPORATION, FOR (i) A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND (ii) AN INCREASE IN ITS WATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.	)	DOCKET NO. W-02500A-10-0382

SURREBUTTAL

TESTIMONY

OF

JUAN C. MANRIQUE

PUBLIC UTILITIES ANALYST I

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

JUNE 13, 2011

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EXECUTIVE SUMMARY
GOODMAN WATER COMPANY
DOCKET NO. W-02500A-10-0382

The Surrebuttal Testimony of Staff witness Juan C. Manrique addresses the following issues:

Capital Structure – Staff continues to recommend that the Commission adopt a capital structure for Goodman Water Company ("Applicant") for this proceeding consisting of 18.6 percent debt and 81.4 percent equity.

Cost of Equity – Staff recommends that the Commission adopt a 9.3 percent return on equity ("ROE") for the Applicant. Staff's estimated ROE for the Applicant is based on cost of equity estimates for the sample companies ranging from 9.2 percent for the discounted cash flow method ("DCF") to 9.3 percent for the capital asset pricing model ("CAPM").

Cost of Debt – Staff continues to recommend, that the Commission adopt an 8.5 percent cost of debt.

Overall Rate of Return – Staff recommends that the Commission adopt an overall rate of return ("ROR") of 9.2 percent.

Response to the Rebuttal Testimony of Applicant's witness Mr. Thomas J. Bourassa - The Commission should reject the Company's proposals to allow for a firm size adjustment and to rely heavily on analysts' forecasts for DCF estimates as well as forecasted U.S. Treasury rates for Historical Market Risk Premium CAPM results.

Response to the Rebuttal Testimony of Applicant's witness Mr. James Schoemperlen – Water utilities have limited access to long-term, low interest refinancing. Accordingly, the Commission should use the Applicant's actual 8.5 percent interest rate as the cost of debt used to determine the rate of return.

I. INTRODUCTION

Q. Please state your name, occupation, and business address.

A. My name is Juan C. Manrique. I am a Public Utilities Analyst employed by the Arizona Corporation Commission ("ACC" or "Commission") in the Utilities Division ("Staff"). My business address is 1200 West Washington Street, Phoenix, Arizona 85007.

Q. Are you the same Juan C. Manrique who filed direct testimony in this case?

A. Yes, I am.

Q. What is the purpose of your Surrebuttal Testimony in this rate proceeding?

A. The purpose of my Surrebuttal Testimony in this rate proceeding is to report on Staff's updated cost of capital analysis with its recommendations regarding Goodman Water Company's ("GWC" or "Applicant") cost of capital and to respond to the cost of capital portion of the rebuttal testimony of GWC's witness Mr. Thomas J. Bourassa ("Mr. Bourassa's Rebuttal").

Q. Please explain how Staff's Surrebuttal Testimony for cost of capital is organized.

A. Staff's surrebuttal testimony for cost of capital is presented in four sections. Section I is this introduction. Section II discusses Staff's updated cost of capital analysis. Section III presents Staff's comments on Mr. Bourassa's rebuttal testimony. Section IV presents Staff's comments on intervenor Mr. Shoemperlen's rebuttal testimony. Lastly, Section V presents Staff's recommendations.

II. COST OF EQUITY AND OVERALL RATE OF RETURN

Q. Did Staff update its analysis concerning the Applicant's cost of equity ("COE") since it filed its Direct Testimony?

A. Yes. Staff updated its analysis to include the most updated data available.

Q. What is Staff's updated COE?

A. Staff's updated COE is 9.3 percent. In Staff's direct testimony, the COE was 9.1 percent.

Q. What is Staff recommending for GWC's COE?

A. Staff is recommending a COE of 9.3 percent derived from its updated cost of equity estimates that range from 9.2 percent to 9.3 percent.

Q. Did Staff update its analysis concerning the Applicant's overall rate of return?

A. Yes.

Q. What is Staff's updated overall rate of return?

A. Staff's updated overall rate of return is 9.2 percent.

Q. What is Staff recommending for GWC's overall rate of return?

A. Staff is recommending an overall rate of return of 9.2 percent. Staff's recommendation is based on a COE of 9.3 percent, a cost of debt of 8.5 percent and a capital structure of 81.4 percent equity and 18.6 percent debt, as shown in Surrebuttal Schedule JCM-1.

III. RESPONSE TO THE REBUTTAL TESTIMONY OF THE APPLICANT'S COST OF CAPITAL WITNESS

Q. Does Staff have a response to Mr. Bourassa's argument that Staff's COE recommendation is too low when compared to the Commission's authorized COE of 10.3 percent in the recent Sahuarita case?[1]

A. Yes. As Mr. Bourassa mentions later in his testimony,[2] Staff's final analysis in the Sahuarita case was done in June of 2010. Since Staff's methodology has not changed in the intervening time, the difference is related completely to changes in investor expectations.

Q. Does Staff have a response to Mr. Bourassa's assertion that "the importance of analyst estimates is that they reflect widely held investor expectations"?[3]

A. Yes. While Mr. Bourassa has demonstrated that these estimates reflect widely-held analyst estimates, it has not been demonstrated that these estimates are widely-held by *investors*. As discussed in my direct testimony, there are numerous published books and articles that cast doubt on the accuracy of research analysts' forecasts.[4] Investors, being keenly aware of these inherent biases in forecasts, will use other methods to assess future growth.

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[1] Mr. Bourassa's Rebuttal page 13.
[2] Mr. Bourassa's Rebuttal page 13, lines 20-22.
[3] Mr. Bourassa's Rebuttal page 18, lines 7-8.
[4] Mr. Manrique's Direct page 37, lines 9-13.

Q. How does Staff respond to Mr. Bourassa's reference to several studies used by Mr. Gary Hayes in a San Diego Gas & Electric case that address whether analysts growth forecasts are overly optimistic?[5]

A. In a more recent article from the McKinsey Quarterly which is published by McKinsey & Company (Attachment A), the authors' state:

> To better understand their (analysts) accuracy, we undertook research nearly a decade ago that produced sobering results. Analysts, we found, were typically overoptimistic, slow to revise their forecasts to reflect new economic conditions, and prone to making increasingly inaccurate forecasts when economic growth declined.

Also:

> Only in years such as 2003 to 2006, when strong economic growth generated actual earnings that caught up with earlier predictions, do forecasts actually hit the mark. This pattern confirms our earlier findings that analysts typically lag behind events in revising their forecasts to reflect new economic conditions...So as economic growth cycles up and down, the actual S&P 500 companies report occasionally coincide with the analysts' forecasts, as they did, for example, in 1988, from 1994 to 1997, and from 2003 to 2006.

What this demonstrates is that, outside of economic boom years, analysts' estimates are overly optimistic. That these estimates occasionally coincide with actual earnings does not disprove the widely held view that analysts' estimates are overly optimistic. One can only conclude that investors have this information and take it into account when making investment decisions.

[5] Mr. Bourassa's Rebuttal page 18 and Exhibit TJB-COC-RB3.

Q. Does Staff have a response to Mr. Bourassa's assertion that firm size is a systematic risk factor[6]?

A. Yes. While firm size may be a factor in COE estimation, it has not been demonstrated that this is true for regulated utilities, therefore Staff rejects this assertion. As previously stated, Staff does not agree that the Company should receive a size risk adjustment.

IV. RESPONSE TO THE REBUTTAL TESTIMONY OF INTERVENOR SCHOEMPERLEN

Q. How does Staff respond to Mr. Schoemperlen's assertion that Staff "cherry picked"[7] the sample companies used as a proxy for GWC's COE estimation in the current case?

A. Staff has chosen these proxy companies due to their characteristics as mainly engaging in regulated water operations and the availability of their financial information. If Staff were "cherry picking" companies in order to bias the COE results, one would expect the sample companies to change frequently over time. Yet, Staff has essentially used the same six companies since, at least, the early 2000's. The only change Staff made was eliminating Philadelphia Suburban and adding Aqua America due to the latter's acquisition of Philadelphia Suburban.

Q. Does Staff have a response to Mr. Schoemperlen's contention that there should be a downward adjustment in GWC's COE due to its less leveraged capital structure?[8]

A. Yes. As previously stated,[9] Staff does not use a financial risk adjustment because GWC is not a publicly-traded company, and thus, it does not have access to the capital markets.

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[6] Mr. Bourassa's Rebuttal, page 24, line 13.
[7] Mr. Shoemperlen's Rebuttal, page 4, line 49.
[8] Mr. Schoemperlen's Rebuttal, page 4, lines 51-56, page 5, lines 76-88
[9] Mr. Manrique's Direct Testimony, page 34, lines 4-5

Q. What is Staff's response to Mr. Schoemperlen's objection to Staff's acceptance of GWC's 8.5 percent cost of debt due to it being held by an affiliate?

A. Water utilities historically have had limited access to long-term debt financing. Even when banks and other lending institutions offer loans to water utilities, the term is relatively short and the interest rate similar to that GWC is experiencing with its existing loan. Although low interest loans are often available from the Water Infrastructure Financing Authority of Arizona ("WIFA") for initial construction, WIFA does not offer refinancing of existing loans. Accordingly, Staff concludes that as 8.5 percent is GWC's actual cost of debt, this is the appropriate cost of debt to use when determining the Company's rate of return.

V. STAFF RECOMMENDATIONS

Q. What are Staff's recommendations for GWC's cost of capital?

A. Staff makes the following recommendations for GWC's cost of capital:

1. Staff recommends a capital structure of 18.6 percent debt and 81.4 percent equity.
2. Staff recommends a cost of debt of 8.5 percent.
3. Staff recommends a cost of equity of 9.3 percent.
4. Staff recommends an overall rate of return of 9.2 percent.

Q. Does this conclude your testimony?

A. Yes, it does.

Goodman Water Company Cost of Capital Calculation
Capital Structure
And Weighted Average Cost of Capital
Staff Recommended and Company Proposed

[A] Description	[B] Weight (%)	[C] Cost	[D] Weighted Cost
Staff Recommended Structure			
Debt	18.6%	8.5%	1.6%
Common Equity	81.4%	9.3%	7.6%
Weighted Average Cost of Capital			**9.2%**
Company Proposed Structure			
Debt	18.3%	8.5%	1.6%
Common Equity	81.7%	10.2%	8.3%
Weighted Average Cost of Capital			**9.9%**

[D] : [B] x [C]
Supporting Schedules: JCM-3 and JCM-4.

Intentionally left blank

Goodman Water Company Cost of Capital Calculation
Final Cost of Equity Estimates
Sample Water Utilities

[A]	[B]		[C]		[D]		[E]
DCF Method			D_1/P_0 [1]	+	g [2]	=	k
Constant Growth DCF Estimate			3.4%	+	5.1%	=	8.5%
Multi-Stage DCF Estimate						=	9.9%
Average of DCF Estimates							**9.2%**
CAPM Method	Rf	+	β [5]	x	(Rp)	=	k
Historical Market Risk Premium[3]	2.5%	+	0.76	x	7.2% [6]	=	8.0%
Current Market Risk Premium[4]	4.3%	+	0.76	x	8.3% [7]	=	10.6%
Average of CAPM Estimates							**9.3%**
					Average		**9.3%**
					Financial risk adjustment		
					Total		**9.3%**

1 MSN Money and Value Line

2 Schedule JCM-8

3 Risk-free rate (Rf) for 5, 7, and 10 year Treasury rates from the U.S. Treasury Department at www.ustreas.gov

4 Risk-free rate (Rf) for *30 Year Treasury bond rate* from the U.S. Treasury Department at www.ustreas.gov

5 Value Line

6 Historical Market Risk Premium (Rp) calculated from Ibbotson Associates SBBI 2009 Yearbook data

7 Testimony

Goodman Water Company Cost of Capital Calculation
Average Capital Structure of Sample Water Utilities

[A]	[B]	[C]	[D]
Company	Debt	Common Equity	Total
American States Water	49.8%	50.2%	100.0%
California Water	53.4%	46.6%	100.0%
Aqua America	57.2%	42.8%	100.0%
Connecticut Water	55.9%	44.1%	100.0%
Middlesex Water	49.4%	50.6%	100.0%
SJW Corp	53.4%	46.6%	100.0%
Average Sample Water Utilities	**53.2%**	**46.8%**	**100.0%**
GWC - Actual Capital Structure	**18.6%**	**81.4%**	**100.0%**

Source:
Sample Water Companies from Value Line

Goodman Water Company Cost of Capital Calculation
Growth in Earnings and Dividends
Sample Water Utilities

[A]	[B]	[C]	[D]	[E]
Company	Dividends Per Share 2000 to 2010 DPS[1]	Dividends Per Share Projected DPS[1]	Earnings Per Share 2000 to 2010 EPS[1,2]	Earnings Per Share Projected EPS[1]
American States Water	1.9%	3.7%	6.2%	2.2%
California Water	0.8%	3.0%	4.0%	4.0%
Aqua America	7.7%	6.0%	6.7%	8.4%
Connecticut Water	1.5%	No Projection	0.9%	No Projection
Middlesex Water	1.8%	No Projection	2.4%	No Projection
SJW Corp	5.2%	3.8%	3.8%	9.1%
Average Sample Water Utilities	**3.2%**	**4.1%**	**4.4%**	**6.0%**

1 Value Line

2 Negative values are inconsistent with the DCF, accordingly, they are excluded from the average.

Goodman Water Company Cost of Capital Calculation
Sustainable Growth
Sample Water Utilities

[A]	[B]	[C]	[D]	[E]	[F]
Company	Retention Growth **2001 to 2010** br	Retention Growth Projected br	Stock Financing Growth vs	Sustainable Growth **2001 to 2010** br + vs	Sustainable Growth Projected br + vs
American States Water	3.1%	6.7%	1.7%	4.9%	8.4%
California Water	2.2%	4.2%	3.8%	6.0%	8.1%
Aqua America	4.5%	5.5%	4.4%	8.9%	9.9%
Connecticut Water	2.3%	No Projection	0.9%	3.2%	No Projection
Middlesex Water	1.3%	No Projection	4.2%	5.4%	No Projection
SJW Corp	3.9%	2.8%	0.1%	4.0%	2.9%
Average Sample Water Utilities	**2.9%**	**4.8%**	**2.5%**	**5.4%**	**7.3%**

[B]: Value Line
[C]: Value Line
[D]: Value Line and MSN Money
[E]: [B]+[D]
[F]: [C]+[D]

Goodman Water Company Cost of Capital Calculation
Selected Financial Data of Sample Water Utilities

[A]	[B]	[C]	[D]	[E]	[F]	[G]
Company	Symbol	Spot Price 5/11/2011	Book Value	Mkt To Book	*Value Line* Beta β	Raw Beta β *raw*
American States Water	AWR	**33.57**	20.36	1.6	**0.75**	0.60
California Water	CWT	**36.75**	21.05	1.7	**0.70**	0.52
Aqua America	WTR	**22.99**	8.65	2.7	**0.65**	0.45
Connecticut Water	CTWS	**25.24**	12.78	2.0	**0.80**	0.67
Middlesex Water	MSEX	**18.62**	10.91	1.7	**0.75**	0.60
SJW Corp	SJW	**22.80**	14.57	1.6	**0.90**	0.82
Average				**1.9**	**0.76**	**0.61**

[C]: Msn Money

[D]: Value Line

[E]: [C] / [D]

[F]: Value Line

[G]: (-0.35 + [F]) / 0.67

Goodman Water Company Cost of Capital Calculation
Calculation of Expected Infinite Annual Growth in Dividends
Sample Water Utilities

[A]	[B]
Description	g
DPS Growth - Historical[1]	3.2%
DPS Growth - Projected[1]	4.1%
EPS Growth - Historical[1]	4.4%
EPS Growth - Projected[1]	6.0%
Sustainable Growth - Historical[2]	5.4%
Sustainable Growth - Projected[2]	7.3%
Average	**5.1%**

1 Schedule JCM-5

2 Schedule JCM-6

Goodman Water Company Cost of Capital Calculation
Multi-Stage DCF Estimates
Sample Water Utilities

[A]	[B]	[C]	[D]	[E]	[F]	[H]	[I]
Company	Current Mkt. Price (P_o)[1]	Projected Dividends[2] (Stage 1 growth) (D_t)				Stage 2 growth[3] (g_n)	Equity Cost Estimate (K)[4]
	5/11/2011	d_1	d_2	d_3	d_4		
American States Water	33.6	1.07	1.12	1.18	1.24	6.6%	9.6%
California Water	36.8	1.28	1.34	1.41	1.48	6.6%	9.9%
Aqua America	23.0	0.64	0.67	0.70	0.74	6.6%	9.2%
Connecticut Water	25.2	0.94	0.99	1.04	1.09	6.6%	10.2%
Middlesex Water	18.6	0.75	0.79	0.83	0.87	6.6%	10.5%
SJW Corp	22.8	0.72	0.75	0.79	0.83	6.6%	9.6%

Average **9.9%**

$$P_0 = \sum_{t=1}^{n} \frac{D_t}{(1+K)^t} + \frac{D_n(1+g_n)}{K-g_n}\left[\frac{1}{(1+K)}\right]^n$$

Where : P_0 = current stock price
D_t = dividends expected during stage 1
K = cost of equity
n = years of non – constant growth
D_n = dividend expected in year n
g_n = constant rate of growth expected after year n

1 [B] see Schedule JCM-7

2 Derived from Value Line Information

3 Average annual growth in GDP 1929 - 2010 in current dollars.

4 Internal Rate of Return of Projected Dividends